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GS ECONOMY

CURRENT ISSUES in INDIAN ECONOMY

Specially designed for UPSC Mains 2014

by

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1. Inflation, RBI and Government's new Monetary Policy Framework

Inflation

The rate at which general level of prices for goods and services is rising and subsequently the purchasing power is falling is termed as inflation.

Inflation & GDP Data (% increase) for the last 10 years

Year	Avg.	13-14	12-13	11-12	10-11	09-10	08-09	07-08	06-07	05-06	04-05
CPI	**8.11**	*9.50*	*10.20*	*8.40*	*10.50*	*12.30*	*9.10*	*6.20*	*6.80*	*4.20*	*3.90*
WPI	**6.49**	*5.90*	*7.50*	*8.80*	*9.60*	*3.60*	*8.00*	*4.80*	*6.50*	*3.70*	*6.50*
GDP	**7.55**	*4.70*	*4.50*	*6.69*	*8.91*	*8.59*	*6.72*	*9.32*	*9.57*	*9.48*	*7.05*

Reasons for high inflation in the Indian economy

Inflation has become sticky in the last few years as can be seen from the above table.
The main reasons that can be attributed for high inflation are:

(i) India has stuck in a position of low growth and high inflation which may be due to a weak government beset by allegations of corruption and policy slowdown, especially in the last few years.

(ii) Out of the total weight-age in CPI, 50% is food and beverages. In the last five years there has been double digit rise in prices of fruits and vegetables and the prices of protein rich food like egg, meat and fish have moved beyond 15%. The main reason for the same is rise in rural incomes, which has grown by over 20% annually over the last five years and is prompting villagers to expand and move towards protein rich diets

(iii) Supply side (cost push) factors have also made the production of food items costly due to the rising prices of fertilizer, diesel, electricity etc.

RBI's (Monetary Policy) role in controlling inflation and its impact on growth

Date	*30th July 08*	*21st April 09*	*25th Oct 11*	*3rd May 13*	*28th Jan 14*	*30th Sept 14*
Repo Rate	*9%*	*4.75%*	*8.5%*	*7.25%*	*8%*	*8%*

After the 2008 financial crisis, RBI started cutting repo rate to provide impetus to growth as can be seen that in a span of just 9 months, RBI reduced the repo rate from 9% (July 08) to 4.75% (April 09). But then suddenly RBI shifted its gear towards controlling inflation (thinking that it is a demand side issue and by increasing the rate, the money supply in the economy will be reduced which will ultimately contain inflation) and started increasing the repo rate through its continuous series of 13 rate hikes which brought repo rate to 8.5% in Oct 11. RBI went wrong here (that inflation is demand side) as in India, inflation has been predominantly a supply side constraint and this aspect blunts effectiveness of monetary policy measures.

With every hike in repo rate, growth started getting retarded as the cost of capital (rate at which a company raises finances) went up. Though RBI has always stated that growth is not linked to cost of capital, the fact remains that small as well as large businesses get hit from the cost of capital. Policy paralysis and international macroeconomic factors added fuel to the fire. Investments started slowing down which had an impact on GDP growth and an economy growing at 9% came back to 6%. Even individuals started feeling a pinch of a high rate of interest in the form of higher EMI and other loan payments.

The credit driven growth of the Indian economy got hit with a series of rate of interest hikes. While RBI thought that rate of interest increases will contain inflation, global factors continued to increase inflation in spite of RBI's rate hikes. RBI had absolutely no control on global factors such as crude oil prices which is dependent on international factors. RBI's attempt to push growth at the cost of controlling inflation produced results but it was temporary. RBI subsequently (much later in May 2013) reduced the repo rate to 7.25% from its peak of 8.5% but it was too late. The economy refused to take off as investment climate had worsened.

The RBI Governor is again following hawkish monetary policy and has not reduced the repo rate since January 2014 (8%), presuming that it will cool down the inflation. The retail inflation measured by CPI has cooled down to 6.46% in September 2014 but it may be due to releasing the supply side bottlenecks.

RBI's activism in initiating monetary policy measures could not bring the desired result because monetary policy alone cannot work as panacea for ills faced by Indian economy. The problem may lie in weak ruling government (till UPA-II) beset by allegations of corruption and policy paralysis.

<u>Difference between Headline and Core Inflation:</u>
Headline inflation measures price inflation that takes into account all types of inflation (i.e. it includes all type of goods and services) that an economy can experience. Unlike headline inflation, core inflation measures the inflation excluding food and energy items. Headline inflation is more useful for the households because it reflects changes in the cost of living.

<u>Urjit Patel Committee Report</u>
The Urjit Patel committee gave its report in January 2014 on improving the efficacy of the present Monetary Policy framework. The following were some of the main recommendations:

1. The headline CPI should be the nominal anchor for monetary policy and the RBI should make this the predominant objective.

   Explanation: RBI's monetary policy has two main objectives of "*moderate inflation*" and "*economic growth*". Other objectives are financial stability and *high* employment. But now this report recommends that RBI shall focus on only "*moderating the inflation"* and leave "*economic growth*" and other objectives as secondary. Further, while earlier RBI was targeting the WPI inflation but now RBI should make "*headline CPI*" index as its main target for monetary policy.

   Current Situation: Accordingly, RBI (and other government agencies) has adopted the new Consumer Price Index (CPI) (combined) as the key measure of inflation.

2. Inflation from the current (January 2014) level of 10 per cent to be brought down to 8 per cent over a period not exceeding the next 12 months (January 2015) and to 6 per cent over a period not exceeding the next 24 month (January 2016). And after that (once it is achieved), the nominal anchor or the target for inflation should be set at 4 per cent with a band of +/- 2 per cent around it.

   Current Situation:
   Keeping the above target in mind RBI has not changed the repo rate (8%) since January 2014 during various monetary policy reviews (RBI reviews monetary policy bi-monthly). Since June 2014, the headline inflation (CPI) has slowed and it was 6.46% in September 2014 which is in line with the set target. But one reason to be not very optimistic is that the cooling of the inflation in the recent months may be due to the base effect.

3. The committee asked the Central Government to ensure that the fiscal deficit as a ratio to Gross Domestic Product is brought down to 3.0 per cent by 2016-17.

New Monetary Policy Framework

The centre has decided to unveil the new monetary policy framework latest by end December 2014. Under the new framework, the government (or the Parliament) will set the new inflation target, while its implementation and setting of interest rates will be with the new monetary policy committee. (*Currently RBI sets the inflation target for its own and tries to achieve it through its monetary policy tools like repo rate etc.)*

The government will set a quantitative moniterable target (of inflation) for a given period and the monetary policy panel headed by RBI governor will then set interest rates to meet the inflation target set by the parliament.

This is in line with the monetary policy framework followed in the US and the UK.

2. Comprehensive Financial Inclusion Plan (CFIP) or *Sampoorn Vittiyea Samaveshan*

What is Financial Inclusion

Financial inclusion is the delivery of financial services which include bank accounts for savings and transactional purposes, low cost credit for productive, personal and other purposes, financial advisory services, and insurance facilities etc. at affordable costs to vast sections of disadvantaged and low income groups.

Financial inclusion broadens the resource base of the financial system by developing a culture of savings among large segment of rural population and plays its own role in the process of economic development. Further, by bringing low income groups within the perimeter of formal banking sector; financial inclusion protects their financial wealth and other resources in critical circumstances. Financial inclusion also mitigates the exploitation of vulnerable sections by the money lenders by facilitating easy access to formal credit.

Background

The Government of India and the Reserve Bank of India have been making concerted efforts to promote financial inclusion as one of the important national objectives of the country. The nationalization of banks in 1969 was the first step towards financial inclusion. Since then, initiatives such as introduction of priority sector lending norms, branch licensing norms with focus on rural/semi-urban branches, no-frills account, easier KYC norms, general credit cards to the poor, lead bank scheme, promoting the use of IT and intermediaries etc, have been undertaken to bring the financially excluded into the ambit of formal financial system.

RBI had set up the Khan Commission in 2004 to look into financial inclusion and the recommendations of the commission were incorporated into mid-term policy review of 2005–06.

Due to RBI's concerted efforts since 2005, the number of branches of Scheduled Commercial Banks increased from 68,681 in March 2006 to 1,02,343 in March 2013, spread across length and breadth of the country. In rural areas, the number of branches increased from 30,572 to 37,953 during March 2006 to March 2013.

As per the Census 2011, of the total 24.67 crore households in the country, 10.19 crore (41%) did not have access to banking services. In rural areas 44% households and in urban area 33% still did not have a bank account.

The UPA financial inclusion push, *Swabhimaan* was started in 2011 and it targeted unbanked villages in a phased manner. Under the new financial inclusion plan, the government is planning to switch the gears from ***'push'*** to ***'pull'***, that is from bank-driven to customer-driven which can be possible only by creating awareness among the financially excluded people about the basic banking facilities.

Pradhan Mantri Jan Dhan Yojana (PMJDY)

On 15th August 2014, the Prime Minister announced his ambitious financial inclusion scheme which was formally launched on 28th August 2014 under the name "Pradhan Mantri Jan Dhan Yojana" to eradicate the financial untouchability from the country

Comprehensive financial inclusion of the excluded sections is proposed to be achieved by 14th August, 2018 in two phases as under

Phase-I (15^{th} August 2014 – 15^{th} August 2015)

- Universal access to banking facilities
- Providing Basic Banking Accounts (no minimum balance requirement) with overdraft facility of Rs. 5000 (after satisfactory completion of one year of operations) and RuPay Debit Card with inbuilt accident insurance cover of Rs. 1 lakh. Those who open accounts by January 26, 2015 will be given an additional life insurance cover of Rs 30,000.
- Creation of Credit Guarantee Fund for coverage of defaults in overdraft accounts. If the overdraft in these accounts goes bad, the government would pay a portion of that from this fund
- Financial Literacy Programme

Phase-II (15^{th} August 2015 – 15^{th} August 2018)

- Micro Insurance
- Unorganized sector Pension schemes like *Swavlamban*

Implementation

PMJDY's first phase will emphasize on universal access to all the beneficiaries to banking services through sub-service areas (SSAs). Each SSA will consist of 1,000-1,500 families in a cluster of villages and each SSA will be serviced by a Banking Correspondent Agent (BCA) who will facilitate account opening and ensure smooth transactions. There would be a shift from focus on geographical area to coverage of households i.e. a shift from supply-side to demand-side.

The government has allowed a number of agencies to operate as Banking Correspondents (BCs) like corporate BCs, Kirana shopkeepers and daak sevaks, in addition to individuals/organizations operating as BCs. RBI is planning to allow the proposed small and payment banks to function as BCs. BCAs to be deployed will be 'sons of the soil' who can win the trust of the rural people. But the success of the BC model will depend on proper remuneration, timely payment, adequate number of transactions and support from the banks. Introducing e-KYC will address the challenge of residence proof which generally hampers rural people in opening bank accounts.

Impact and Benefits

- Indians spend around 2% of GDP in gold purchases. If every Indian household has a bank account then rather than saving in gold, they will start keeping money in bank accounts (opened under Jan Dhan Yojana). And if 50% of the gold spending (i.e. 1% of GDP) is converted into savings in bank accounts then ultimately this saving is turned into productive investments by bank lending to various projects. India's Incremental Capital Output Ratio (ICOR) is around 4.5 for the last 15 years, so 1% investment will lead to 0.22% extra increase in GDP *(ICOR = % Investment/ % change in GDP)*.

- The NDA government has started transferring LPG subsidy through Direct Benefit Transfer (DBT) scheme. Under this scheme the first option will be to get the DBT through Aadhaar linked bank accounts but if people don't have Aadhaar cards then they can simply link their bank accounts (opened under Jan Dhan Yojana) with their LPG account numbers. It is expected that it will help government to save Rs. 10,000 crore in FY 2015. The use of DBT for various social welfare schemes like PDS, MNREGA etc. through the bank accounts will help the government to save Rs. 30,000 crores in leakages by FY 2019.
  (*Earlier the UPA government had started DBT scheme for LPG in June 2013 but discontinued it in January 2014 after a Supreme Court order which said that Aadhaar numbers should not be mandatory for transfer of funds under welfare schemes)*

Challenges

There are two parts to financial inclusion. One part is getting the network of physical infrastructure in place – Banks, BCs, ATMs, power, digital connectivity etc. while the second part is getting the unbanked to use the services confidently and frequently. So just putting in place the first part will not work. More than 15 crore accounts were opened under the previous mission, of which RBI recognizes half as dormant. While 24X7 power and digital connectivity have to be reliable for ensuring transactions, agents and banks have to find the business viable to keep them going. Getting account holders to use the banking services and ensuring the agents to stay in the system is the real challenge.

The government needs to address the last-mile challenges, sort out the Aadhaar imbroglio, target increasing transactions per agent, provide budgetary support to process timely DBT payments with appropriate share to the agents and clearly communicate to all stakeholders, including the customer, about the exact payment processes and the usage of accounts, etc.

3. Tax Administration Reforms Commission (TARC)

Introduction

The then Finance Minister P. Chidambaram in his Budget Speech of 2013-14 had announced a proposal for setting up of Tax Administration Reform Commission (TARC) to review the application of tax policies and tax laws in India in the context of global best practices, and to recommend measures for reforms required in tax administration. Accordingly, TARC was established in August, 2013. The term of the Commission is 18 months and would work as an advisory body to the Ministry of Finance. The Commission comprises a Chairman (Dr. Parthasarathi Shome), two full time members and four part time members. The Commission submitted its first set of recommendations to the Ministry of Finance on 30th May 2014.

Need for TARC (A background of India's Tax Administration situation)

The Centre's tax-to-GDP ratio, which had come close to 12% during FY08 following the tremendous growth of over 9% before the 2008 financial crisis has been gradually falling and touched 9% by FY12. It stands at around 10% in FY14 despite all efforts to revamp revenue collection. The problem lies in lax tax administration and mounting disputes. Close to 4 lakh tax cases are locked up in various courts even though the success rate of the taxman (inspector or collector of taxes i.e. govt.) is one-fifth or less in case of direct tax cases and close to a tenth for indirect tax cases. Not surprisingly, tax arrears are on the rise, leading to lower realization from taxpayers. On top of this the retrospective taxation and other deterrents have dented investor confidence.

TARC Recommendations

TARC has listed its recommendations in the belief that they can be implemented if the willpower exists at the top policy level. Such changes have occurred in other countries as well. TARC has said that the recommendations should be considered as a package and not on a pick-and-choose mode which would not work. The following are the recommendations:

(i) Customer Focus

- Trained officers and staff and a dedicated unit in the government for delivery of taxpayer services.
- Spend at least 10% of the tax administration's budget on taxpayer services
- All the individuals shall be provided with pre-filled returns with options to modifications

(ii) Structure and Governance

- Club Central Board of Direct Taxes (CBDT) and Central Board of Excise and Customs (CBEC) into a unified Central Board of Direct and Indirect Taxes.

- Tax administration needs to have greater functional and financial autonomy and independence from governmental structures.
- Abolition of the post of revenue secretary to empower the Board of taxes and the income tax department to carry out their responsibilities efficiently.

(iii) People Function

- Complete overhaul of recruitment and evaluation practices of tax administration staff.

(iv) Dispute Management

- Avoid retrospective amendment as a principle.
- Launch a special drive for review and disposal of cases currently clogging the system by setting up dedicated task forces.
- Disputes must get resolved in a timeframe and if not then the case in question would lapse in favor of the taxpayer.

(v) Key Internal Processes

- PAN should be developed as a common business identification number (CBIN) to be used by other government departments also.
- Refunds should be granted within a strict time frame
- Streamline scrutiny and scrap manual TDS filing for returns.

(vi) Information and Communication Technology

- Achieve a fully digitized environment wherein everyone from the top leader to the last person on the frontline works in a digital environment.

Comment

TARC has comprehensively analyzed the ills plaguing the tax administration and made some eminently desirable recommendations, which will result in improving the tax-to-GDP ratio by ensuring that honest taxpayers are not unduly harassed and are encouraged to continue to comply with the law. Implementation of these recommendations will also simultaneously ensure that dishonest taxpayers get extra attention which they deserve from the tax administration by suitably empowering the tax administration with use of technology and global best practices.

4. WTO's Bali Summit – Agriculture, Peace Clause & Trade Facilitation Agreement (TFA)

The Ninth Ministerial Conference of the WTO was held in Bali from 3rd to 7th December 2013. The Bali package included three things:

- Agriculture
- Trade Facilitation
- Least Developed Countries

1. Agriculture (Agreement on Agriculture)

The main objective of this agreement is to discipline and reduce domestic support (subsidies) given to agriculture while at the same time giving freedom to the member countries in designing their domestic agricultural policies with respect to their specific needs.

The nature of the domestic support given by a government can be divided into two categories:

- Support with no or minimal distortive effect on trade ("Green Box")
  (exempted/ allowed under WTO)

- Support that distorts trade ("Amber Box")
  (restricted under WTO)

WTO classifies all the domestic support into three categories. *The above two categories and a third one which is basically distorting in nature but the distortion in trade is very less in value and hence WTO allows/exempts it.*

Domestic Support

allowed under WTO	*allowed under WTO*	*restricted under WTO*
1. **Green Box:** R&D support, infra support like irrigation, electricity, expenses related to accumulation & holding of public stocks for food security, domestic food aid to the section of population in need and any direct payment to producers which is not linked to production, i.e. no production is required to receive such payment.	2. **Other exempted measures:** Development Measures: Investment subsidies, agriculture input subsidies to low income or resource poor producers. Blue Box: payments made on fixed areas or number. of livestock. Production is required to receive the payment but actual payment not linked to production. De-minimis Support (explained below)	3. **Amber Box** Any support which does not fall in the 1st or 2nd category is subject to reduction commitments. The WTO members should try to reduce this type of support.

Total Aggregate Measurement of Support (AMS): It includes all product-specific support (price support, input subsidies) and non-product specific support (interest subsidy). Price support is calculated by multiplying the quantity of production with the difference between the administered price (in India it is Minimum Support Price) and the external reference price (world market price). In similar way any kind of support (fertilizer subsidy and others) is calculated by the difference of administered price and the market price. For a developing country if the total AMS is less than 10% then there is no penalty and comes under "**De-minimis support**" under point 2 above, but if it is more than 10% then it will come under point 3 above and the countries must try to bring it under 10% (for a developed country this cap is 5%).

"India's apprehension is that its total AMS may exceed 10% of the permitted cap."

There is also an obligation that all members of WTO must notify the Committee on Agriculture (in WTO) the extent of their domestic support measures under Green Box, other exempt measures, Blue Box and non-exempt support and their AMS calculations.

India had not notified about its domestic support and AMS to the WTO since a decade. It had provided information to WTO only till FY 2003-04. In September 2014, India notified to WTO all its domestic support from FY 2004-05 to 2010-11, which says that its total AMS is way below the 10% cap. But some may raise the issue over the calculation of AMS as there is no real data on how much subsidy goes to rich farmers (non-exempt) and how much goes to poor farmers (exempt under domestic support, point 2 above).

Peace Clause: During the Bali Conference, the member countries agreed to a "peace clause" which refers to a time period during which the member countries would refrain from seeking penalty against countries which still breach the 10% domestic support (total AMS) cap.

The 'peace clause' said that no country would be legally barred from food security programmes even if the subsidy breached the limits (10%) specified in the WTO Agreement on Agriculture. It is an interim measure which prevents any WTO member from challenging any developing country for crossing the 10% subsidy cap. This 'peace clause' is expected to be in force for four years until December 2017. The package also said that members should work on a permanent solution to reach an agreement by December 2017.

Countries including India fear that the peace clause would expire by December 2017 and if a permanent solution is not reached by then, then their subsidy programme may be challenged by the other WTO members. That is why they want an amendment to the Bali agreement to specify that *"the peace clause would last till a permanent solution is found".*

2. **<u>Trade facilitation Agreement (TFA):</u>**

This agreement aims to simplify customs rules across all international borders for faster movement of goods and services. The Agreement contains provisions for faster and more efficient customs procedures through effective cooperation between customs and other appropriate authorities on trade facilitation and customs compliance issues. It also contains provisions for technical assistance and capacity building in this area.

Under this agreement, each member shall:

- publish its laws, rules and regulations related to import and export procedures, rates of taxes and duties, penalties in easily accessible manner
- make available on internet the forms and documents required for import and export and contact information on enquiry points
- adopt procedures allowing the option of electronic payment for duties, taxes, fees and charges collected by customs incurred upon import and export
- provide for release of perishable goods within shortest possible time

It is being believed, especially by the proponents of the agreement that the TFA once signed could add $1 trillion to global GDP and also can generate 21 million jobs by slashing red tape and streamlining customs procedures.

The deadline to sign the agreement was 31st July 2014, and the deal has to come into force fully by 2015.

India blocked the TFA (to keep its bargaining power) in the last week of July 2014, fearing that the "peace clause" will expire by December 2017 and if a permanent solution is not reached by then regarding domestic support then its subsidies may be challenged by WTO members. It says that WTO shall first suggest a permanent solution to the domestic support issue then only it will sign the TFA.

3. **<u>Least Developed Countries (LDC):</u>**

The WTO member countries should give preferential treatment to the products of LDC i.e. allowing Duty Free and Quota Free (DFQF) Market Access for products originating from LDCs (i.e. products that are being exported from LDCs to advanced and developing countries).

5. WTO - Compulsory Licenses

Introduction

A patent is a right granted to the owner of an invention that prevents others from making, using, importing or selling the invention without the owner's permission. This right is granted by the government. A patentable invention can be a product or a process that gives a new technical solution to a problem. It can also be a new method of doing things or the composition of a new product.

Patents are a kind of Intellectual Property Rights which are granted for 20 years to the inventor. The inventors can also use this right to negotiate payment in return for others using this right. These rights motivate the people for new innovations and research.

TRIPS and (India's) Patent Act 1970

Trade Related Aspects of Intellectual Property Rights (TRIPS) came into effect from January 1st 1995 (with the establishment of WTO) and the deadline for complying with TRIPS obligations for India (a developing country) was January 1st 2005. The Patents Act, 1970 (of India) was amended to make it fully TRIPS compliant by 2005. The Patents Act 1970, as enacted originally, contained a provision for grant of a compulsory license. However, in the Patents (Amendment) Act 2002, the provisions related to compulsory license was substituted with a completely new one (section 84) and by the Patents (Amendment) Act, 2005 *product* patents were allowed to be granted for drugs, which was not allowed under the 1970 Act. As per the 1970 Act only *process* patenting was allowed which means patenting of the method of manufacturing a product.

Compulsory Licenses

If a government authority has granted patent to someone (person or entity) in its own country then WTO's TRIPS agreement says that each other member country (government) will have to give protection to the patent right of the fellow member. *(This means if a country A has granted patent to someone in country A then all other member countries of WTO will have to give the same patent right to the person or entity of country A)*

But WTO also provides a reasonable restriction on the rights of the patent holder under certain circumstances. This restriction is provided by allowing other member countries to enact provisions for granting Compulsory Licenses to prevent the abuse of patent right. *Compulsory licensing means that the government allows someone else to produce the patented product or process without the consent of the patent owner.*

Article 31 of the TRIPS agreement says that Compulsory Licenses can be granted broadly in two cases:

- The person or company applying for a compulsory license must have tried to negotiate a voluntary license from the patent holder on reasonable commercial terms. Only if that fails can a compulsory license be issued

- and even when a compulsory license has been issued, the patent owner will receive payment and “the right holder shall be paid adequate remuneration in the circumstances of each case, taking into account the economic value of the authorization/right”

All those countries who are members of WTO have complied with TRIPS agreement by amending their own patent laws. Similarly India has also amended its patent laws.

The Patents Act 1970 (after amendments in 2002 and 2005) says that application for grant of Compulsory Licenses on Patents can be made any time after the expiration of three years from the date of the grant of the Patent to the Controller General of Patents on the basis of the following grounds:

- That the reasonable requirements of the public with respect to the patented invention have not been satisfied, or
- That the patented invention is not available to the public at a reasonably affordable price, or
- That the patented invention is not worked(supplied/produced) in the territory of India

Case Study of Bayer Corporation (USA) vs. Natco Pharma (Hyderabad, India)

Bayer Corporation (“Bayer”) invented the drug called “Sorafenib” useful in the treatment of advanced stage liver and kidney cancer in 1990s. Bayer first applied for a patent in the United States Patent and Trade Mark Office in 1999 and subsequently filed an International Application on 12th January 2000. Bayer entered the national phase (a follow up to know whether there is already such drug or not) in India in July 2001. After an examination under the provisions of the Patents Act 1970, a patent was granted on 03.03.2008 *(Bayer had already obtained Patents in many other countries for the same drug by 2008)*.

Bayer developed the drug and launched it in 2005 under the trade name “Nexavar” for treatment of kidney cancer and in 2007 for treatment of liver cancer. Bayer received the regulatory approval for importing and marketing the drug in India and launched it in India in the year 2008.

Natco Pharmaceuticals (“Natco”) is a reputed Indian generic drug manufacturer. Natco has developed the *process* to manufacture this drug and received a license from the Drug Controller General of India for manufacturing the drug in bulk and for marketing it in 2011.

The drug “Nexavar” is not a life saving drug, but a life extending drug i.e. in case of kidney cancer, the life of a patient can be extended by 4 to 5 years, while in case of liver cancer the life of a patient can be extended by 6 to 8 months. The drug has to be taken by the patient throughout his lifetime and the cost of therapy is Rs. 2, 80,428/- per month.

In 2008, Bayer did not import the drug in India at all, while in 2009 and 2010, Bayer imported in small quantities which was grossly inadequate. Bayer imports and sells the drug in India but has not taken adequate steps to manufacture the product in India to make full use of the invention. The drug is exorbitantly priced and out of reach of most of the people in India.

Bayer launched the product all over the world in 2006 and made huge sales which have grown by leaps and bounds every year. But Bayer clearly neglected the Indian market and did not launch in India until 2009. The Patent was granted in 2008 and from then till 2011, Bayer did not bother to fulfill the demand to comply with the duty imposed by the Patent Act. Bayer only imports the drug into the Indian market and does not manufacture the drug by itself in India, though it does manufacture and sell other products in India.

Natco approached Bayer with a request for a voluntary license (in return of some payment to Bayer) to manufacture and sell the drug in India at a price of Rs. 8800/- for one month therapy but it did not materialize. Natco filed an Application for grant of Compulsory License on 29.07.2011 under Section 84 (1) of the Patents Act 1970. Three years had lapsed since the date of grant of patent to Bayer when this Application by Natco was filed.

In view of the above facts, the Controller General of Patents opined that *"the reasonable requirements of the public with respect to the patented invention have not been satisfied. The pricing adopted by Bayer is exorbitant for its patented life saving product and is an abuse of its monopolistic rights and such practice is unfair and anti-competitive. It was concluded that the patented invention was not available to the public at a reasonably affordable price and consequently a Compulsory License must be issued to the Applicant."*

Finally on March 9 2012, Compulsory License was granted under section 84 of the Patents Act 1970 to Natco by the Controller General of Patents on the following terms & conditions.

(i) The price of the drug covered by the Patent, sold by Natco shall not exceed Rs. 8800/- for one month's treatment

(ii) Natco shall have the right to manufacture the drug only at his own manufacturing facility and shall not outsource the production. Natco shall not have the right to import the drug covered by the patent

(iii) The license is non exclusive and non assignable (to somebody else)

(iv) The license has been granted solely for the purpose of making, using and selling the drug covered by the patent for the purpose of treating liver and kidney cancer in humans within the territory of India

(v) Natco shall pay royalty at the rate of 6% of the net sales of the drug to Bayer

(vi) Natco's product must be visibly distinct from the Bayer's product (eg color and or shape), the trade name (Nexavar) must be distinct and the packaging must be distinct. Bayer will provide no legal, regulatory, medical, technical or any other support of any kind to Natco

<u>Special 301 Report:</u> The US Trade Representative (USTR) conducts annual review of Intellectual Property laws of its partner countries. The USTR in its "Special 301 report" of 2014 has identified India as a "priority watch country" as it thinks that India has failed to protect US's intellectual property rights. Through this measure, US may create pressure on India to increase IPR protection. This step by the US has not gone down well with the Indian government.

6. Smart Cities

On 10th July 2014, the Finance Minister in his budget speech of 2014-15 allocated a sum of Rs. 7,060 crore (for FY 2014-15) for the development of 100 smart cities in the country. Smart Cities come under ministry of Urban Development, Government of India.

Introduction:

In India, the urban population is currently 31% (40 crores) of the total population (130 crores) and it contributes over 60% of India's GDP. It is projected that in the next 15 years i.e. by 2030 urban population will touch 60 crores and will contribute nearly 75% of the national GDP. Cities are accordingly referred to as the engines of economic growth. There is accordingly a crying need for the cities to get smarter to handle this large-scale urbanization and finding new ways to manage complexity, increase efficiency, reduce expenses, and improve quality of life.

Identifying the 100 Smart Cities:

The experience from all over the world suggests that developing Greenfield (totally new) cities as smart cities has not been successful as a city can grow on a sustainable basis only if there are opportunities for economic activity, entertainment, education, health care and a wide range of such services.

The following cities can be chosen for development as smart cities in India:

- One satellite city (NOIDA is a satellite city of Delhi) of each of the cities with a population of more than 40 lakhs (9 cities)
- All the cities in the population range of 10 to 40 lakhs (44)
- All state/UT capitals even if their population is less than 10 lakhs (17)
- Cities of tourist and religious importance (10)
- Cities in the 5 to 10 lakhs population range (20)

What is a Smart City?

People migrate to cities primarily for employment. To support their happy and comfortable living, they also need good quality housing, cost efficient physical and social infrastructure such as water, sanitation, electricity, clean air, education, health care, security, entertainment, etc. Industries also locate in cities because there are agglomeration economies (benefits that firms obtain by locating near each other) that provide easy access to labour and other factors of production. In this context, Smart Cities are those that are able to attract investments. Good infrastructure, simple and transparent online processes that make it easy to establish an enterprise and run it efficiently are important features of an investor friendly city. Without this a city loses attraction as an investment destination. An investor is considered as someone who helps a city rather than someone who only profits from it. *Thus, the key features of a smart city are quality of life and employment and investment opportunities.*

Some examples of smart cities from the world are Seoul, Singapore, Yokohama and Barcelona.

Pillars of a smart city

The three pillars on which a smart city rests are:

- Institutional Infrastructure – It refers to the activities that relate to the planning and management systems in a city. It include the systems of governance, safety and security, information and communication technology (ICT) based speedy service delivery, banking/financial institutions, transparency and accountability, public participation in governance and decision making etc.

- Physical Infrastructure – It refers to the stock of physical infrastructure such as transportation system, housing stock, energy system, power supply system, water supply system, sewerage system, waste management system, drainage system etc. which are all integrated through the technology.
  Mobility is at the core of a smart city which emphasizes walking, cycling and public transport systems as the primary means for mobility with personal motor vehicles being actively discouraged.

- Social Infrastructure – It relates to those that work towards developing the human and social capital such as educational, healthcare, entertainment systems etc.

These together determine the quality of life in a city.

Financing of Smart Cities:

Funding of the smart cities will depend on whether it is a green filed project involving building of the city from scratch or upgrading an existing city to meet minimum smart standards (brown field project). The investment in green field smart cities can be significantly higher than the brown field. In most green-field projects, bulk of the financial resources are mobilized through sale of land or built-up commercial or residential space, with user charges helping meet recurring operations & maintenance costs. In the case of existing cities, on the other hand, user charges constitute the primary means of servicing the investments made since the scope for new residential/commercial space development is usually limited. Additional user charges can be levied on various utilities like water supply and power supply, charges on fuel purchase, registration of property etc to fund the brown field smart city investments.

Public Private Partnership can be a mode for building the smart cities.

7. Real Estate Investment Trusts (REITs)

On 10th July 2014, Finance Minister in his budget speech of 2014-15 said that "Real Estate Investment Trusts" (REITs) will soon be allowed. Securities and Exchange Board of India on 11th August 2014 issued guidelines under which REITs were allowed to operate in India.

Definition of REITS:

A "Real estate investment trust" is a trust registered under the Indian Trusts Act, 1882 or a "Real estate investment management company" incorporated under the Companies Act, 1956 which manages a fund/ corpus where the funds are invested in real estate property. *(From further on in this article, Real Estate Investment Trust and Real Estate Investment Management Company will be collectively called REITs)*

The term is confusing and seems like only trusts have the authority to manage (invest in) such funds but actually any company which has business in real estate is also allowed to manage such funds and are collectively called REITs.

REIT is like a mutual fund but it deals only in real estate investments. REITs are investment vehicles that mobilize money from investors and invest it in real estate.

How REITs work:

Suppose there is a REIT and it wants to invest the funds that it has into a real estate property, then the minimum amount of this fund shall be at least Rs. 500 crores. Or simply the assets of the REITs should be at least Rs. 500 crores. Then it can go for an initial public offer (to raise additional money from the general public) and the minimum fund that it is allowed to raise from the public is Rs. 250 crores. Generally the REITs can raise the funds from the public/ market only once and the number of shares to be offered is fixed that means it is a closed ended fund. The public will be allotted number of shares/ units depending on how much money they have put in (invested) and these units will then be traded on a stock exchange. There will be no further issue of units and if somebody wants to purchase the units then he can do so by purchasing it from the initial buyers. The minimum public holding will be 25% (of the total value of the REIT) and an investor will have to put in a minimum of Rs. 2 lakhs and the trading lot will be at least Rs. 1 lakh.

Salient features of REITs:

- The funds can be managed by real estate investment trusts (REITS) or real estate investment management companies.

- These funds can be invested only in commercial real estate properties/ assets.

- At least 80 per cent of the money mobilized by a REIT has to be invested in completed revenue-generating properties, while 20% can be put in developing properties (under construction projects), real estate stocks, bonds and government securities.

- The source of income for the REIT investors is the rental income from the real estate property and capital appreciation.

- All REITs will have to distribute 90% of their income (rental and other income) as dividend to the investors

Benefits to the Investors

- REITs will make the expensive real estate sector accessible to the middle-class investor.

- Most middle-class investors do not invest in commercial real estate because of the big size of investment. This entry barrier will be removed with the launch of REITs (A investor can invest a minimum of Rs 2 lakhs)

- Owning property is beset with many problems such as verifying authenticity of deeds and records, registration, payment of stamp duty, property tax, etc. REITs remove all these hassles.

- Investors will have an opportunity to diversify their investment in various projects.

- Income from REITs will be inflation adjusted since rental income will go up with inflation.

- Complete tax pass-through will be available for REITs. This means that the income generated will be taxed in the hands of the investors, and that the fund itself (REIT) will not have to pay any tax on the same, eliminating the possibility of double taxation. (Unlike in the case of a company, the company needs to pay tax on profit and when the profit is distributed to the shareholders as dividend then company again needs to pay Dividend Distribution Tax to government before distributing dividend)

Benefit to the Real Estate Sector

- The benefits to the real estate industry, currently plagued with problems such as weak demand, cash constraints, etc., can be tremendous. As of now, real estate developers use their own funds and bank loans to develop their property. In a weak demand scenario, reduced cash flow creates problems with the viability and profitability of the project. Once REITs are launched, the scenario will change as developers will be able to sell the property to REITs and move on to execution of new projects.

- It also has the potential to revive the real estate market and contribute substantially to employment generation and economic growth of the country.

SEBI has also cleared ***Infrastructure Investment Trusts (InvITs)*** *along with REITs which are very similar to REITs but are for infrastructure sector in general.*

8. "Make in India" – Future of Manufacturing

"Make in India" is PM's signature initiative launched on 25th September 2014 to offer red carpet to investors from India and abroad to invest in India.

Percentage share in country's GDP of various sectors (2012-13)

Agriculture	Industry			Services
Agriculture & forestry	Mining & quarrying	Manufacturing	Electricity, gas, water supply etc	Construction, real estate, transport etc.
14%	2%	15%	2%	67%

Introduction:

"Make in India" contains a vast number of proposals including easier norms and rules designed to get foreign companies to set up shop and make the country a manufacturing powerhouse.

The programme lays emphasis on 25 sectors with focus on job creation and skill enhancement. These sectors include: automobiles, automobile components, aviation, bio-technology, chemicals, construction, defense manufacturing, electrical machinery, electronic systems, food processing, IT & Business Process Management, leather, media and entertainment, mining, oil & gas, pharmaceuticals, ports, railways, renewable energy, roads & highways, space, textiles and garments, thermal power, tourism & hospitality & wellness.

As part of the make in India campaign, foreign investment ceilings in construction sector will be eased to enable greater participation in the government's 100 smart cities project and affordable housing sector. FDI caps in railways and defense production have already been eased to 100% and 49% respectively.

Why focus on manufacturing

India's unique positioning in the global marketplace as a services-led economy is in contrast to most other developing economies, including China, which took the traditional route of labour-intensive manufacturing followed up by higher value added part-labour, part-capital intensive manufacturing. In India, while the services sector – employing decently skilled English-speaking workers – has had its share of glory, it cannot provide employment to the large masses. At present, 12 million people enter the Indian workforce each year. A substantial part of them is low skilled workers, many having migrated from rural India to the urban centers. Jobs are not being created at a proportionate pace. During 2005-12 India added only 15 million jobs, a quarter of the figure added in the previous six years. *The scale and nature of employment that is required to employ these people with limited skills and education can only be provided by mid- and low-end manufacturing.*

After India liberalized its economy in 1991, the services sector was among the fastest growing part of the economy, contributing significantly to GDP, economic growth, international trade and investment. Manufacturing contributes just 15 percent to India's GDP, compared to a 67% percent contribution by services. Exports in manufacturing are performing well but most of it remains in the skill-intensive sector like automotive, engineering, etc. This does nothing for the large population of low-skilled workers who are either unemployed or labouring away in hazardous, inhumane conditions beyond the purview of established formal state regulations.

India ranks a lowly 134 out of 189 countries in the World Bank's "ease of doing business" index in 2014. It slipped three places from its 2013 rank. Global investors have always been criticizing about complex rules and bureaucratic red tape that delay investment decisions.

Initiatives taken by the government for "make in India"

(i) The government has set up an investor facilitation cell "Invest India", which will act as the first reference point for guiding foreign investors on all aspects of regulatory and policy issues and to assist them in obtaining regulatory clearances.

(ii) A dedicated cell has been created to answer queries from business entities through a newly created web portal www.makeinindia.com

(iii) The ministry of home affairs has been asked to give all security clearances to investment proposals within 3 months.

(iv) All central government services are being integrated with an e-Biz single window online portal.

(v) The campaign is simultaneously being launched in different state capitals including Mumbai, Chennai and Bangalore. "The idea is to involve states through a hub-and spoke model"

(vi) The initiative will also target top companies across sectors in identified countries.

(vii) An advisory has been sent to all departments/state governments to simplify and rationalize regulatory environment which includes online filing of all returns in a unified form.

(viii) With a view to providing flexibility in working hours and increased intake of apprentices for on the job training, the government is in the process of amending various labour laws.

9. Inverted Duty Structure and its impact on domestic manufacturers

Definition:

Inverted Duty Structure is a situation in which the import (customs) duty on a finished product is lower than the import duty on the raw materials or intermediate products used in the manufacture of that finished product.

The existence of Inverted Duty Structure puts the domestic manufacturing industry in a situation of disadvantage. Due to inverted duty structure domestically produced goods become costly (those dependent on imported raw materials and intermediate goods) because of the high tariff on imported raw material and intermediate products used in the production. And because of that domestically manufactured goods are not able to compete against the cheaper imported finished goods in the domestic market. As a result, domestic value addition suffers and if not corrected, such a structure can lead to a total wipe out of the domestic industry.

Inverted Duty Structure can result if duty reduction is done only for a certain stage in the entire product chain and the other stages are left untouched. This could also result from Free Trade Agreements (FTAs) signed between India and its partner countries in which duty concessions are provided for specific products from the other country.

Impact on Domestic Manufacturing Sector

Nine manufacturing sectors in India have reported duty inversion including aluminium products, capital goods, cement, chemicals, electronics, paper, steel, textiles and tyres.

Inverted duty structure in tyre sector exists with respect to natural rubber, which is the principal raw material for manufacturing. The basic customs duty on tyres is 10 per cent and under various trade pacts (FTAs), the duty ranges between nil to 8.6%, facilitating tyre imports into India while on natural rubber the duty is 20 per cent or Rs 20/kg (whichever is lower).

During the April-March period of 2013-14, the manufacturing sector's output contracted 0.8 per cent as compared with 1.3 per cent growth in the previous year.

Finance Minister in his budget presentation on 10th July 2014 for FY 2014-15 reduced customs duties on various items (like coal tar, steel grade limestone etc.) to address the issue of inverted duty structure and boost the domestic manufacturing sector. But no steps have been taken to alter the inverted duty structure in the case of tyre industry.

10. FDI in Railways and its impact on economic growth

Department of Industrial Policy and Promotion (DIPP), Ministry of Commerce and Industry, on 27th August 2014 notified Foreign Direct Investment (FDI) norms for the railways sector. The government allowed 100% FDI through automatic route in railways in *construction and maintenance* of the following areas:

- High speed train projects
- Dedicated freight lines/ corridors
- Mass rapid transport systems
- Railway electrification and signaling systems
- Passenger and freight terminals
- Rolling stock including train sets, locomotives or coach manufacturing and maintenance facilities
- Suburban corridor projects through public private partnership
- Infrastructure in industrial park pertaining to railway lines and connectivity to main railway lines

(FDI is not allowed in train operations and safety)

Impact on Economic growth:

The Indian Railways' current model (government owned and operated) was "unsustainable" and had "little" hope for "modernization". The foreign investment in railways was first mooted in December 2012 by UPA government but was pending since then. The new government's approval of liberalizing the railways sector is expected to help in modernization and expansion of the railways which will bring in a significant engine of inclusive growth and development for the country and can potentially contribute an additional 1.5 - 2% to the country's GDP.

Railways are a capital intensive (huge amount of funds are required for development) sector and its growth depends heavily on availability of funds for investment in rail infrastructure. Internal revenue sources (profit generated from Indian railway) and government funding through budget are insufficient to meet the requirement of this capital intensive sector. Currently Indian Railways is facing a cash crunch of about Rs. 30,000 crores to complete pending projects and is expecting foreign funds on easy repayment terms for several segments.

India is expecting a substantial chunk of foreign direct investment in railways sector to come from China and Japan.

With the government giving nod for FDI, the proposed "Mumbai-Ahmedabad High Speed Rail Corridor project" is expected to get a push for which the approximate cost is around 65,000 crores. The electric locomotive factory at Madhepura and diesel locomotive factory at Marwhora in Bihar are also expected to get a boost.

11. Role of PPP in India's infrastructure development & challenges

Introduction

Public Private Partnership (PPP) is defined as a partnership between a government body and one or more private parties, where the government enters into a long term contract with the private partner to deliver a good or service, and the private partner is responsible for building, operating and maintaining the assets that are necessary for delivering the service to either government or individuals. In a PPP project, some responsibilities and risks are borne by the government and some by the private party. The division of risks and responsibilities between the parties depend on the party managing it most efficiently. Hence, PPP fills a space between fully government and fully private way of executing and maintaining a project.

The PPPs were introduced in early 1990s which redefined the roles of public and private sectors in public service delivery. Generally a Special Purpose Vehicle (SPVs are companies which are formed to execute a specific project) is formed to execute and maintain such a project.

Role of PPP in Infrastructure Development

Infrastructure projects are very capital intensive and require huge funds for their execution. Governments of various countries introduced PPPs because they had the potential of bringing in private finance to public service delivery and private players could deliver the services more efficiently i.e. at least cost with better quality. Many governments experienced the pressure of fiscal deficits and increasing public debt burdens by the mid-1990s and they found the private finance more alluring, especially for large infrastructure projects.

The private sector in India is quite large and possesses huge financial and technical resources. The private sector can very well complement the government sector in execution and delivery of large infrastructure projects through public private partnership. In a country which is debt ridden and which has budget constraints, the private sector can play a pivotal role with its huge financial resources. But private participation in the process of infrastructure development through PPP is fraught with various hurdles and challenges. While private telecom services is a success story in India, the PPP constitutes a miniscule share in overall infrastructure building despite initiation of various policy adjustments and sector-specific reform programmes.

Stable macroeconomic framework, sound regulatory structure, investor friendly policies, sustainable project revenues, transparency and consistency of policies, effective regulation and liberalization of labour laws, and good corporate governance are the basic requirements, which define the success of the PPP model. As we lack in providing the above environment, the status of the PPP in the infrastructure development in India, both in the Central Government schemes as well as State sponsored schemes, is not encouraging.

<u>Challenges in PPP in India:</u>

1. <u>Regulatory Environment</u>: There is no independent PPP regulator as of now. As provision of many public assets and/ or related services has natural monopolistic characteristics, the same shall be regulated to ensure that the interests of users and service providers are protected taking into consideration the affordability of the users and certainty of pricing and revenue stream to the private party.

2. <u>Lack of Information</u>: The PPP program lacks a comprehensive database regarding the projects/ studies to be awarded under PPP. An online data base, consisting of all the project documents including feasibility reports, contract agreements and status of various clearances and land acquisition will be helpful to all bidders.

3. <u>Project Development</u>: The project development activities such as detailed feasibility study, land acquisition, environmental/ forest clearances etc. are not given adequate importance by the government authorities. The absence of adequate project development by authorities leads to reduced interest by the private sector, mispricing and many times delays at the time of execution.

4. <u>Lack of institutional capacity</u>: The limited institutional capacity to undertake large and complex projects at various Central ministries and especially at state and local body's level hinder the translation of targets into projects.

5. <u>Financing availability</u>: The private sector is dependent upon commercial banks to raise debt (loan) for the PPP projects. With commercial banks reaching the sectoral exposure limits, and large Indian Infrastructure companies being highly leveraged (debt ridden), funding the PPP projects is getting difficult.

6. <u>Standardization of Contract:</u> The agreement to be entered into between government and the private party should be standardized. That is, we should have a model contract agreement for all the sectors detailing in terms and conditions regarding standard clauses like dispute resolution, termination, financing etc. It will help inject international best practices and avoid each time writing a new contract for every new PPP project and will save cost and time. Lack of standard contracts/ clauses that are approved by the center makes bureaucrats more reluctant to sign off on PPP deals.

12. PPP projects & investment models in various sectors

BOT: Build Operate Transfer (private party builds the project, operates it and then transfers the project to the government authority at the end of the contract period) *BOOT: Build Own Operate Transfer (private party is also the owner of the assets of the project)*

Road: The road projects are mainly built on the following three models:

(i) Engineering Procurement and Construction (EPC) model: The government gives the contract only to build the road to a private contractor based on submission of the tender by the party at the lowest cost. Private party builds the road and hands it over to the government who then maintains the road. *(It is not a PPP model)*

(ii) Toll based BOT/BOOT projects: The private party is selected to build, maintain and operate the road based on the party submitting the tender for maximum sharing of toll revenue to the government. In case the revenue from toll is expected to be not enough to cover the cost of the project then the government gives one time support in terms of upfront grant called Viability Gap Funding (VGF) and the private party is selected based on who asks for minimum VGF. All the traffic and commercial risk lies with the private party as the private party is dependent on toll for its revenues. *(It is a PPP model)*

(iii) Annuity based BOT/BOOT projects: The private party is selected to build, maintain and operate the road project based on the party submitting the tender asking for minimum annual payment (each year) from the government for the entire term of the contract. The private party recovers all the cost of construction and maintenance of the project from the government annually and there is no traffic and commercial risk to the private party. These are such projects where govt. does not expect to collect toll. *(It is a PPP model)*

The Delhi-Noida Direct (DND) Flyway is one of the first PPP project based on Build Own Operate Transfer (BOOT) model. It is an eight-laned 9.2 Km access controlled tolled expressway connecting Delhi to Noida. The project was won by Infrastructure Leasing and Financial Services (IL&FS) and is being operated through a Special Purpose Vehicle called "The Noida Toll Bridge Company Ltd." The expressway was opened to public in 2001.

Railway:

PPP in railway is mainly for Dedicated Freight Corridors (DFC) and sandwiched new lines and gauge conversion projects.

When a section of the railway line is built on PPP model then all the clearances and land acquisition is done by Indian railway (IR) and design, build, construction & maintenance of the track is done by the private player. Freight is collected by the Indian Railway (IR) and 50% of the freight of that section is given by IR to the private party. The private party is selected through tendering process. If 50% of the freight (which is going to the private party) is not expected to cover the full construction and maintenance cost then the private party will ask for Viability Gap Funding from IR and that private party which asks for minimum funding will be selected. If 50% of the freight is expected to cover the full construction and maintenance cost then that private party will be selected which will give the maximum premium (funds) to the IR.

Ministry of Railways has established "Dedicated Freight Corridor Corporation of India Ltd." in 2006, a Special Purpose Vehicle for planning, development, mobilization of financial resources and construction, maintenance and operation of the eastern and western DFCs.

Eastern Corridor: Ludhiana – Mugalsarai- Sonnagar-Kolkata (1835 Km)
Ludhihana-Mugalsarai section funded by World Bank
Mugalsarai-Sonnagar section funded by Ministry of Railway
Sonnagar-Kolkatta section funded by **PPP**

Western Corridor: Delhi – Rewari – Vadodara – Mumbai (1483 Km) (funded by Japan)

The total cost of the two corridors is approx. Rs. 80,000 crore and is expected to be completed by 2017-18.
There will be centralized control of operations on the DFC and double stacking containers will be running along these corridors. The operation and maintenance cost is expected to be half on DFC as compared with present IR network. It has been planned to build multimodal logistics park along the corridors to provide complete transport solutions to the customers.

Airport:

The Airports Authority of India (AAI) was established in 1995 under the provision of Airport Authority of India Act 1994 for management of all airports in India by a single authority. AAI under the Ministry of Civil Aviation is responsible for creating, upgrading, maintaining and managing civil aviation infrastructure in India. AAI manages 15 international airports, 8 customs airports, 25 civil enclaves, and 80 domestic airports.

AAI Act was amended to provide legal framework for airport privatization. PPP in airports started in 2005-06 with the award of the Delhi and Mumbai airport to the private parties GMR and GVK respectively. The private parties were given the responsibilities to make new investments in the airport infrastructure facilities and to operate and maintain the airport.

The source of revenue for an airport operator is landing charges, parking charges, passenger service fee, cargo handling, advertising, rentals etc. AAI selects a private party (airport operator) for operation and maintenance of an airport based on which party commits to pay maximum percentage of these revenues to the AAI. Earlier AAI used to operate and maintain the airports and used to collect these revenues but once the operation and maintenance contract is given to a private party (operator) then they collect these revenues and share with the government.

Port:

There are 13 Major Ports (defined as those owned/controlled by Central government) and around 187 Minor Ports (either owned by State government or private parties) in the country. Ministry of Shipping, Government of India issued guidelines for PPP to bring in new private players in the Major Ports sector in 1996. The objective was to attract private investment as well as to improve efficiency, productivity, quality of service and bring in competitiveness in port services in India. The private players were invited to build and operate the additional new Terminals in the existing Major Ports. (A port is like a railway station at which there are a number of Terminals like the platforms at a railway station. The ships come at a Terminal of a port and load/unload the cargo like the trains come at a platform and passengers get on/off the train).

The source of revenue for a port operator is the charges that it collects from the ships which come and load/ unload their cargo at the ports. The main features of PPP guidelines were:

- That private player is selected which quotes the maximum share of revenue that it will give/surrender to the central government

- The period of contract will be 30 years for which the private player will build and operate the Terminal and after that it will handover that terminal to the government

- Build Operate Transfer (BOT) and Build Own Operate Transfer (BOOT) models were followed for public private partnership projects

The first PPP in Major Ports was for the Jawaharlal Nehru Port Trust (JNPT) in Mumbai. Bids were invited to build a new Terminal (of 600 meter length) at JNPT on Build Operate Transfer (BOT) model for 30 years contract. M/s P & O Ports, Australia won the bid but later it was acquired by DP World. DP World formed a new company Nhava Sheva International Container Terminal (NSICT), the Special Purpose Vehicle (SPV) to build and operate the Terminal. The Terminal became operational in 1999 and its capacity was 7.2 million tonnes of cargo per annum which was further increased to 15.6 million tonnes per year.

Power:

Ministry of Power in association with Central Electricity Regulatory Commission (CERC) and Power Finance Corporation (PFC) has launched an initiative for the development of coal based Ultra Mega Power Projects (UMPP). There are 16 UMPPs of 4000 MW capacity each under the plan out of which 4 have already been awarded to the developers (one to Tata and three to Reliance). The projects are being developed under Public Private Partnership (PPP) with Build Own Operate (BOO) model. PFC is the nodal agency and manages the award of the project to private developers. PFC gets all the clearances done like water, environment, forest, land acquisition and then awards the project to the private developer through two stage tendering process. The private party who commits to sell the power generated from the UMPPs to the government (distribution companies) at the lowest cost per unit is selected as the successful bidder.

13. “Coalgate” and impact of Supreme Court’s verdict on the economy

Coal Statistics for FY 2013-14 (in Million Tonnes)

Coal India Ltd. production	Others production	Import	Total consumption
462	109	169	740

Introduction

“Coalgate” is shorthand for coal block allocation scam. In 1993, the central government began giving coal blocks to government and private companies for captive use. *Captive use means the coal from the allocated coal blocks could only be used by these companies for their specified power projects, steel plants, etc. The sale of coal from these coal blocks was not permitted*. The process of allocation to the government and private companies, however, was flawed. Coal blocks, as the CAG said, were given free to these companies resulting in the block-owners making windfall (super normal) gains. Further, the functioning of the screening committee which evaluated applications to allocate the coal blocks to the companies was opaque and subjective and without any clear criteria. Some companies got far more coal blocks than they needed. Companies with political links got multiple blocks while more deserving candidates did not get any.

On September 24, 2014 Supreme Court (SC) cancelled the 214 captive coal blocks allocated to the companies since 1993 out of the total 218 blocks terming it as illegal. In its judgment declaring the allocations illegal, the Supreme Court said “*The Screening Committee has never been consistent, it has not been transparent, there is no proper application of mind, it has acted on no material in many cases, relevant factors have seldom been its guiding factors, there was no transparency and guidelines have seldom guided it."*

Impact on the Economy

Out of the total 214 coal blocks cancelled by the SC, 42 blocks were under production, producing approximately 53 MT a year and till 31st March 2014 had produced 205 MT.

- Due to this cancellation the coal import bill will go up by Rs. 18,000 crore which will increase the current account deficit (CAD) for the FY 2015.

- The total investments including the coal blocks and its end use power and steel plants is approximately Rs. 2.87 lakh crores which are now at risk. Out of this, more than 1 lakh crore has been financed by the various banks and carries a risk of turning into Non-Performing Assets (NPAs).

- As per the penalty of Rs. 295 per tonne (on 42 producing mines), the companies will have to cough up approximately Rs. 6000 crores on their previous production.

All this combined will inflate the cost of power and steel and fan inflation.

14. <u>Gas Pricing Issue and KG-D6 Block</u>

Introduction
Government of India opened up hydrocarbon (oil & gas) exploration and production sector in the country to the private players in 1991. For few initial years small and medium size blocks were offered to private players which were followed by giving bigger blocks since 1997-98 as per the New Exploration and Licensing Policy (NELP).

NELP: Under this policy government auctions oil and gas blocks to PSU's and private companies. First government identifies blocks of oil and gas reserves with some degree of certainty of finding reserves and then it auctions the blocks. When the private or the government company wins the block (during auction) then it does complete exploration to know whether the extraction of oil and gas reserves will be economically/ commercially viable or not. If on exploration the company finds it feasible then it develops the block (installation of platforms and other machinery for extraction of oil and gas) and starts production. *(If on exploration the company finds that it would not be feasible to extract oil or gas from the block then it surrenders the block to the government and loses the investment)*

Under NELP, auctioning happens in phases/rounds. Till now nine rounds of auctioning has happened under NELP starting from the first in 1999. Total 254 blocks have been awarded and 154 are in operation i.e. under production.

Basis on which the companies are selected:
During the auction, the company needs to quote how much percentage of oil/gas it will give to the government out of the total extracted oil/gas. The company which will quote the maximum percentage wins the block. Once a company wins the block, an agreement is signed between the company and the Govt. of India detailing in the terms and conditions for the entire period. This agreement is called Production Sharing Contract (PSC).

The sharing of oil/gas to the government starts only after the company has recovered its *costs of exploration, development and production* (called "Cost Petroleum"). That means till the time the company has not started generating profit, it need not share the oil/gas to the government. (For example, in the first year of production, all the value of oil/gas produced may be utilized to recover cost and hence, the company need not share the oil/gas to the govt.). Once the company has recovered the Cost Petroleum, it will start generating profit called "Profit Petroleum" which is basically the total value of petroleum produced minus Cost Petroleum. Out of the Profit Petroleum, the company needs to share the percentage with the government depending on what it had quoted during the auctioning process.

This model is called "Profit Sharing" in which sharing does not start till there is a profit. The other variant is "Revenue Sharing" under which the private company needs to share the revenues derived from the sale of gas from the first year of production without being affected by whether the company is making a profit or loss.

A case study of KG-D6 Block

Krishna Godavari (KG) Basin is spread across 50,000 Sq Km near the coast of Andhra Pradesh. Reliance Industries Ltd. (RIL) got the D6 block in KG basin (called the KG-D6 block) during the first round of NELP bidding in 1999. And after that a Production Sharing Contract (PSC) was signed between RIL and Govt. of India regarding the terms and conditions and the percentage sharing of gas with the government.

Gas Price Issue:

Reliance can recover the Cost Petroleum from the value of gas produced (Quantity multiplied by price). The price is important for Reliance for two reasons

- Higher price will help RIL to recover its Cost Petroleum in the very initial years
- Higher price will fetch reliance higher value for its share of Profit Petroleum

"So the whole dispute is what will be the price of gas produced from KG D6 block"

The PSC says that the price of gas discovered will be equivalent to market price (also called arms length price) but it shall be approved by the government of India. In 2007 the Empowered Group of Ministers (EGoM) headed by Pranab Mukherjee approved a price of \$4.2 per mmbtu (million metric british thermal unit) which was applicable till 31st March 2014.

RIL began production of gas from KG-D6 block in April 2009 and was charging a price of \$ 4.2 per mmbtu as per EGoM's decision which was due for revision on 1st April 2014.

When RIL got the block it was estimated that the gas production from the block would be 40 mmscmd (million metric standard cubic meters per day) but after that the target was revised to 80 mmscmd. But actual production after reaching a peak of 69.4 mmscmd in March 2010 started declining and in Dec 2013 it reached to a low of 10 mmscmd. Reliance said that the decrease in production is due to technical faults but the government has ***alleged*** *that it may be a* ***deliberate*** *action and a committee has been appointed to investigate the matter.*

Now, RIL claims that at a price of \$4.2, it would be difficult to make new investments and dig more wells to increase the production and wants a revision in price.

The cabinet approved a formula devised by C Rangarajan (former RBI Governor) in 2013 to double the price of gas to \$8.4 per mmbtu with effect from 1st April 2014 and Reliance (and other gas producers) was to get this price but the decision was deferred due to elections in May 2014. But the new NDA government has notified (on 18th Oct 2014) a new price of \$5.61 per mmbtu with effect from 1st November 2014.

Comment: Technically, the gas price should be dependent on the cost of production which depends on how deep are the reserves and what is the geology of the strata. But C Rangarajan had linked the gas price with international gas indices and import price in India. The firms should not be allowed to take windfall (excessive) gains by linking the prices with international prices and weightage must be given to the cost of production. As cement, fertilizer, power plants use this gas; \$8.4 price would have resulted in inflation in economy.

15. Indian Agriculture – Performance and challenges

Period	1951 - 1966	1966 - 1981	1981 - 1992	1992 - 2005	2005 - 2013
Agri-GDP (% growth)	2.1%	3.03%	3.45%	3.14%	3.89%

"Growth in agriculture is critical for any economy as research has revealed that GDP growth originating in agriculture is at least twice as effective in reducing poverty as GDP growth originating outside agriculture".

Performance of Indian agriculture since independence

1951-1966:
Economic planning in this period was mainly marked by industrial growth-led development strategy. The main emphasis was on industry while agriculture received little attention. Some investments were made in agricultural infrastructure, irrigation and electricity. Food requirements were largely met through PL-480 imports from USA. The major source of agricultural growth during this period was area increase without notable productivity gains.

1966-1981:
With major food shortages in the 1960s (droughts and wars), food self sufficiency evolved as a major goal of policy planning. Inputs such as irrigation, fertilizer, power and credit were subsidized to boost the green revolution. Provision of output support in the form of Minimum Support Prices (MSP) was started. Many important institutions such as Commission for Agriculture Cost and Prices (CACP), Food Corporation of India (FCI) and National Dairy Development Board (NDDB) were established and large investments were also made in agricultural research and development. These policies were immensely successful and by the mid seventies India had become self sufficient in the production of food grains and impressive gains had been made in production of milk and sugar. Major source of growth during this period was increase in productivity.

1981-1992
This period was the best phase for Indian agriculture as growth was achieved with inter-regional equity. With self-sufficiency in food grains, focus shifted in this phase to oilseeds and pulses in which growth had lagged behind. Technology Mission in Oilseeds and Pulses (TMOP) was started in 1986. These policy initiatives resulted in very impressive increase in production of oilseeds.

1992-2004
This phase is marked by the launching of macro economic reforms in 1991 and import liberalization in edible oils sector in 1994. Because of the structural changes in the economy there was an improvement in Terms of Trade (ToT) for agriculture. While the improvement in ToT had a slight positive effect on private investment in agriculture, the rising fiscal deficits, on the other hand, contributed to a decline in public investment in agriculture which resulted in decline in profitability of most of the crops.

2005-2013

In this phase, efforts were made to address the issues of declining public investment in agriculture, improving farmer's income, increasing food production and providing economic access to food to large sections of population.

Rashtriya Krishi Vikas Yojana was started in 2007 mainly with the objectives of incentivizing states to increase investment in agriculture (state subject) and use this investment to address the basic needs of farmers.

The National Food Security Mission was launched in 2007 with the limited objective of increasing the production of rice, wheat and pulses by 10, 8 and 2 million tonnes respectively by FY 2012.

The National Food Security Act 2013 was enacted with the main objective of providing economic access to food.

Issues/Challenges:

1. Subsidy vs Investment

   The total pubic (govt.) expenditure on agriculture includes both public investment as well as input subsidies. Agriculture receives public resources more in the form of subsidies than investment. Almost 80 percent is in the form of subsidies and only 20 per cent is investment. Given the budgetary constraints, there is always a trade-off between allocating money through subsidies and increasing investments. Subsidies, unless they are well targeted and are for a limited period, are not equitable and efficient and crowd out public investment in agriculture research, irrigation, rural roads and power. There is an inherent moral hazard in the use of subsidized inputs such as fertilizer and water and their excessive use leads to deterioration in the water table and soil creating an environmentally unsustainable system. Investments take time to fructify but result in sustainable and higher growth.

2. Lagging research and development

   Lack of breakthrough in research and development is one of the main reasons for the decline of productivity in the nineties. India stands poorly in productivity levels when compared with major producing countries. Since there is hardly any scope for further expansion of area under cultivation, the future production prospects depends largely on the improvements in the yield levels.

3. Imbalanced use of fertilizers

   The recommended dose of fertilizer for healthy soil is 4:2:1 for Nitrogen, Phosphorus and Potassium i.e. NPK. Consequent to the decontrol of prices of phosphorus and Potassium (Rs. 24000 per tonne approx.), there was a decline in the application of these fertilizers and increase in the use of Nitrogen (Urea) fertilizer because it is highly subsidized (Rs 5360 per tonne approx.). There are clear indications that the skewed price regime has led to the imbalanced used of N, P & K fertilizers and has deteriorated the soil conditions and raised questions on the environmental sustainability.

4. <u>Soil degradation and over exploitation of ground water</u>

   The emergence of rice-wheat cropping system in states like Punjab, Haryana and western UP, on account of continuous increase in procurement (MSP) prices has resulted in over-exploitation of natural resource base. Study has found that soil health is deteriorating in these areas which is a major cause of decline or stagnation in productivity of cereals particularly wheat and rice.

Comment:

Indian agriculture has the potential to grow at 5 per cent per annum for the next ten years if the government takes bold policy decisions. If the new government can reorient the resources from *subsidies* to *investments* then it will be rewarded handsomely in a political economy and will be a win-win situation for the country as well, as it will accelerate agricultural growth to above 5 percent and will reduce poverty faster.

16. APMC Act and Food Inflation

Agricultural Produce Marketing Committee (APMC) Act

Agricultural Markets in most parts of the country are established and regulated under the State APMC Acts. The whole geographical area in a State is divided into various market areas/ mandis wherein each market will be managed by a Market Committee constituted by the State Government. Once a particular area is declared a market area and falls under the jurisdiction of a Market Committee, no person or agency is allowed freely to carry on wholesale marketing activities outside the market. The wholesalers, retail traders (retail chains like reliance fresh etc) or food processing companies cannot purchase the farm output directly from the farmers, rather they need to purchase from these established mandis and the farmers also need to sell their produce in these mandis.

Salient features of APMC Act

(i) For a trader to operate in a Mandi, he has to get a license for which he must have a shop or warehouse in the Mandi

(ii) The price of the farmers' produce shall be discovered through auctioning so that farmers get a good price of their produce

How APMC Act has exploited the farmers and consumers

(i) Getting a license involves paying bribes and leads to corruption

(ii) Auctioning does not take place and even if it happens, the traders in these mandis form a cartel and collectively keep the prices low ultimately hurting the farmers. During the peak season when the traders buy from farmers at low prices, they don't reduce the prices to final consumers and during the lean season when consumer prices are high, traders don't pass it to farmers

(iii) The government declares minimum support prices (MSP) for many cereal, pulses and oilseeds crops so that the middleman at APMC mandis cannot exploit the farmers beyond a level (otherwise the farmer can sell it at MSP to the government). But for fruits and vegetables government doesn't declare minimum support prices (MSP) which gives plenty of opportunity for the middleman to exploit farmer as well as end consumer.

After so many years of exploitation of farmers and consumers, Ministry of Agriculture drafted a new model APMC Act in 2003 and has asked the state governments to adopt it (as agriculture is a state subject, so states need to reform their laws).

Salient features of new Model APMC Act

(i) Farmer doesn't need to bring his produce to APMC Mandi. He can directly sell it to whomsoever he wants.

(ii) Farm Processors, exporters, graders, packers, etc. can buy agricultural produce directly from farmers.

(iii) It permits Private Market Yards, Direct Purchase Centers, farmers' market for doing trade in agriculture produce.

So far only 16 states have adopted the Model APMC Act because of the Middleman/trader lobbying and various other reasons. Model APMC Act is not 'uniformly' adopted and states have made their own modifications.

For example, Delhi govt. issued a notification on 2nd Sept 2014 to allow wholesale trading of farm produce outside the existing APMC markets of Azadpur, Kehsopur and Shahdara. Azadpur APMC is the biggest mandi of fruits and vegetables in the country and handles more than 4000 tonnes of perishable agricultural commodities that is supplied to all northern Indian states.

Reasons for high food inflation

(i) Import duties on most fruits and vegetables are about 30% (apples, for instance, attract 50% import duty), skimmed milk powder attracts 60% (above the in-quota tariff of 15%), and chicken legs (cut pieces) attract 100%.

(ii) Supply side (cost push) factors have also made the production of food items costly due to the rising prices of fertilizer, diesel, electricity etc.

(iii) High fiscal deficit is one of the root causes of expanding demand more than supplies, and putting pressure on food prices.

Steps taken by the new NDA govt. to tackle food inflation

(i) Central government has planned to liquidate (sale) 15 million tonnes of grains (5 million tonnes of rice and 10 million tonnes of wheat) from Food Corporation of India (FCI) stocks in FY 2015 (the process has already been started)

(ii) On 2nd July 2014, government brought onions and potatoes under the Essential Commodities Act 1955 for one year to curb hoarding. *This will enable state governments to impose limits on the quantity of onions and potatoes that individuals and wholesale traders can stockpile*

(iii) The central government has advised states to de-list fruits and vegetables from the APMC Act

(iv) Central government increased the Minimum Export Price (MEP) for onions at \$500/tonne (from \$300/tonne) and potatoes at \$450/tonne.

Further steps that can help in tackling food inflation

(i) Develop more cold storage facilities so that there is a better matching of supplies with demand, besides saving on wastages.

(ii) Imports should be kept open at low duties.

(iii) Since the rural areas are highly deficient in power, developing a cold chain is difficult and costly affair so compressing the value chain by directly buying from the farmer groups can reduce transaction costs and decrease the food prices.

17. The Right to Fair Compensation and Transparency in Land Acquisition, Rehabilitation and Resettlement Act 2013

Introduction

Under the Constitution of India, “land” falls under the state list while “land acquisition” comes under the concurrent list empowering the centre as well as the states to legislate on the matter. But the states have to frame their laws in conformity with the central legislations and in case of any conflict; the central law prevails over the state’s law.

The original Land Acquisition Act 1894 was a colonial legislation enacted by the British primarily to acquire private land to lay railway lines and for other such construction works. When India got its independence, this Act remained in force and was being used by the government although with few amendments till 31st December 2013.

The Right to Fair Compensation and Transparency in Land Acquisition, Rehabilitation and Resettlement Act 2013 (shortly “LA Act 2013”) came into force on 1st January 2014, while the President had given his assent on 26th September 2013.

Eminent Domain

It is the power the government has to obtain the property of an individual even without the person’s full consent. This allows the government to seize land to be used in public enterprises such as roads, schools or utilities and the landowner will be compensated for the land at fair market value. Government uses this eminent domain power for all forceful acquisitions of land.

Public Purpose

The following category of projects comes under public purpose:

(a) For strategic purposes relating to naval, military, air force including central paramilitary forces or any work vital to national security

(b) For infrastructure projects like railways, highways, roads, ports, power plants, industrial corridors, mining, agro processing, warehousing, government aided or administered educational and research institutions excluding private hospitals, private educational institutions and private hotels

(c) Projects for project affected families

(d) Project for residential purposes for the poor and landless etc.

Applicability

The LA Act 2013 applies in the following conditions:

(i) When the appropriate (Central or State) govt. acquires land for its own use, hold and control (including Public Sector Undertakings) for public purpose

(ii) When the appropriate govt. acquires land for Public Private Partnership projects (ownership of land lies with the government) for public purpose on the condition that prior consent of at least 70% of the project affected families have been obtained

(iii) When the appropriate government acquires land for private companies for public purpose on the condition that prior consent of at least 80% of the project affected families have been obtained

Salient Features:

The following are some important features of the new LA Act 2013

(i) Compensation: It is equal to the Market Value of land and immovable property multiplied by a factor of 1 in case of urban land and multiplied by 2 in case of rural land. In case the land lies between urban and rural area then the multiplying factor will be between 1 and 2 depending on the distance of the project from the urban area.
In addition to the above a "Solatium" (compensation for emotional attachment) equal to 100% of the above compensation shall also be given. So the total compensation stands out to be twice the Market Value for urban area and four times the market value for rural area.

(ii) Social Impact Assessment (SIA): Whenever the government intends to acquire land, it shall consult the Panchayat, Municipality as the case may be in the affected area and carry out an SIA study in consultation with them and it shall make available the report to the general public. The report shall include the number of project affected families, displaced families, whether the proposed acquisition serves pubic purpose etc.

(iii) Rehabilitation and Resettlement (R&R): The project affected families shall be provided with the following in addition to the compensation mentioned in point (i) above:

- A job (where job is created) or onetime payment of five lakhs per affected family or annuity payment of Rs. 2000 (monthly and linked to CPI) for twenty years

- One time "Resettlement Allowance" of Rs. 50,000/- for each affected family

- Each affected family shall get monthly subsistence allowance of Rs. 3000/- for one year

- In case of displacement if a house is lost, the person should be provided with constructed house

<u>Loopholes and Criticisms</u>

(i) Existing projects in which land acquisition process was underway would be affected if they have to recommence the acquisition process under the new LA Act 2013

(ii) The consent of 80% of affected families is quite high and may stall the land acquisition process for the project

(iii) The possibility of land acquisition would be known from the time of the Social Impact Assessment (SIA) process which implies there could be sale of land in the vicinity from the time of the SIA till the issue of preliminary notification (first SIA happens then the government issues preliminary notification for land acquisition). As the compensation for land is linked to actual transactions in the last three years prior to the preliminary notification, these sales during the SIA process may increase the prices of land

The provisions of the new LA Act 2013 do not apply to thirteen existing legislations that provide for acquisition of land in specific sectors for example "National Highway Act 1956", "Land Acquisition (Mines) Act 1885", "The Railways Act 1989" and so on. But whether the land is acquired under the new LA Act 2013 or under the 13 existing legislations, the compensation shall be in line with the new LA Act 2013.

<u>Comment:</u>

The new LA Act 2013 has sought to streamline the land acquisition procedure, bring about greater transparency and safeguard the rights of land owners to be compensated and rehabilitated. In setting out to achieve a balance between promoting industrial growth and ensuring the rights of landowners, the new LA Act 2013 slant towards the protection of land owner's rights.

18. Labour Laws and its impact on economic growth

Introduction

As per the Constitution of India, labour is a concurrent subject. There are in total 44 labour laws that Centre has enacted which are categorized into three types:

(i) 16 can be enforced both by the Centre and states, including the Industrial Disputes Act, Contract Labour Act, Apprentice Act and Minimum Wages Act.
(ii) Another 16 laws are enforced specifically by states, including the Factories Act, Trade Unions Act, Employment Exchange Act and Unorganized Workers' Social Security Act.
(iii) The rest 12 laws are enforced exclusively by the Centre, including the Employee's Provident Fund Act, Employee's State Insurance Act and Mines Act.

Indian labour laws were conceived in the pre-independence period or shortly afterwards based on an import-substitution and statist (state intervention and control) model of economic development. The object of formulating the labour laws was laudable but the changing economic environment has made them outdated. The paradigm has shifted towards global competition, productivity, efficiency and mutual cooperation. The country needs new laws which provide safety standards, caters to the basic needs of workers, take care of their welfare and are flexible enough to create rather than destroy jobs.

Issues with the current laws and impact on economy

India needs to create 80 million jobs during the next 10 years while at present it has created only two million jobs every year during 2005-12. Almost five million persons lost jobs in the labour intensive manufacturing like the textiles and apparels and electronics during 2005-10. According to Goldman Sachs, it is because firms are substituting capital for labour largely because of fear of coming into the ambit of a large number of labour laws.

The Industrial Disputes Act 1947 (ID Act) states that an employer cannot layoff or retrench any worker or close down operations of the establishment without prior permission from the appropriate government. According to employers and economists it has been a major bottleneck of employment generation in the organized sector.

The ID Act (through an amendment made in mid 1980s) requires that any firm employing more than 100 workers needs to get permission from the state government before retrenching workers. In view of these rigidities, the employers have been resorting to technology upgradation with the intention of keeping their workforce below 100. The clause relating to applicability of the ID Act has kept the Indian enterprises small. *According to them, the average number of workers in Indian firms in the organized sector is 75, compared to 178 in Indonesia and 191 in China. The Government of India's Economic Survey (2012- 13) stated that it could be due to the outdated labour laws.*

The ID Act has probably done more to hold back the growth of India's manufacturing sector than any other policy. What is remarkable about this and so many other Indian labour laws (like the Contract Labour Act 1970) is that they leave no room for free contracting. Suppose a firm wants to manufacture a product that has volatile demand - like fashion garments. This firm may want to offer workers higher wages but make it clear to them that they could be given a month's notice and asked to leave. Such a contract will have no legal standing because the ID Act says in advance how and when workers may or may not be retrenched. Similarly the Contract Labour Act says that contract labour can be employed only for activities which are peripheral in nature and does not form core activity of an organization. This creates restriction for companies hiring contract labor for their core activity.

At first sight this law looks like a kind piece of legislation that protects the jobs of poor workers. But what this popular view misses out on is the fact that this law also keeps hundreds of thousands of workers unemployed because firms, wary of the fact that they will not be able to fire them, do not hire in the first place. Also, in areas of volatile demand, many firms have not even come into existence because they realize that India's current legal regime makes them non viable. Labour data from the 1980s shows that the number of people employed in firms of size greater than 100 workers has gone down. This is market's natural response to the amendment in the mid-1980s. *So what is needed is not freedom to firms to deliberately fire workers but a legal regime whereby firms can write different kinds of contracts with their workers depending on their needs. One firm may offer a low wage and lifetime guarantee of work and another a high wage and very short notice to quit.*

It has been found that less rigid nations have more efficient economies, higher wages and a smaller share of labourers who are long-term unemployed. An injection of flexibility in labour market regulation can attract foreign capital, create jobs and unleash higher growth.

Reforms proposed by the NDA govt. (July 2014)

The labour ministry has proposed various reforms in the labour laws which may be put up in the winter session of the Parliament for its approval.

- In Factories Act, the labour ministry proposes to allow companies to hire women workers for night shifts while doubling the overtime to 100 hours in a quarter.
- In Apprentices Act, a labour ministry note said the proposal is to enhance the scope of apprenticeship training to all graduates in various fields such as BA, B Com and B Sc. other than those having a technical education from ITIs or engineering colleges.
- ID Act mandates prior notice for a strike only for public utility services which means workers in "other industries can go on a lightning strike even without a single day prior notice". Labour ministry is considering proposing a small change in Section 22 of the ID Act to moderate strikes and ensure a better work culture.

Comment

The Indian labour laws form a crisscrossing network of chaotic, strangulating, outdated, overlapping and often-contradictory laws that are crying out for urgent overhaul. Given that the reform of labour laws is, contrary to popular perception, in the interests of the workers, what government needs to do is have this topic debated and explained so that workers, instead of opposing such reform, become its advocate. But the reforms will also require complementary policies for providing social security and welfare to workers.