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MAINS 365

Economy

Classroom Study Material 2019

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ECONOMY

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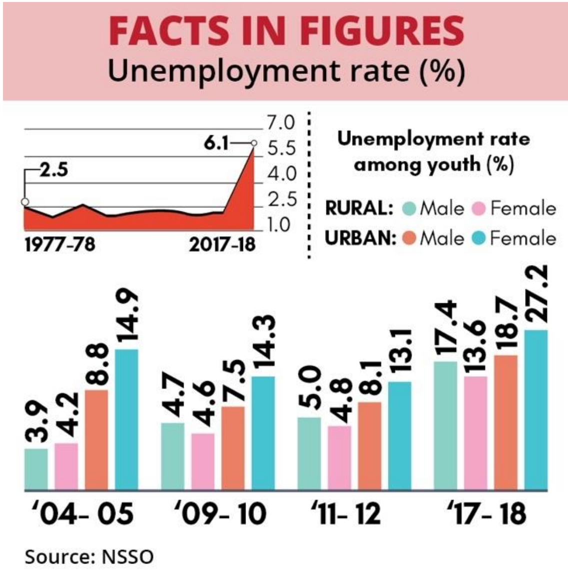
1. EMPLOYMENT, SKILL DEVELOPMENT AND LABOUR REFORMS

1.1. UNEMPLOYMENT AND SKILL DEVELOPMENT

Introduction

Employment Scenario



- **Findings of Periodic Labour Force Survey (PLFS)**
  - The **Labour Force Participation Rate (LFPR)** in India has **declined to 36.9%** in 2017-18 from 39.5% in 2011-12 (NSSO) as per usual status.
    - ✓ **Rural areas:** LFPR declined by 3.6 %
    - ✓ **Urban areas:** LFPR declined by 0.1%
  - The **Worker Population Ratio (WPR)** in India has declined to 34.7% in 2017- 18 from 38.6% in 2011-12 (NSSO).
    - ✓ **Rural areas:** WPR declined by 4.9%.
    - ✓ **Urban areas:** WPR declined by 1.6%.
  - **Gender Gap**- 71% of men above 15 years and above are a part of the workforce as compared to just 22 per cent woman.
    - ✓ Meghalaya is the only state where 50% of the female population is at work while states like Bihar have just 4 % employed women.
  - **Condition in decent employment**- Decent employment has three key indicators i.e. written jobs contract, paid leave and social security benefits. There has been a decline in two of these indicators, as-
    - ✓ The share of **workers with a written job contract in non-agricultural sector** has declined from 40.9% in 2004-05 to 28.9% in 2017-18.
    - ✓ The share of **workers who are eligible for paid leave in non-agricultural sector** has declined from 53.8% in 2004-05 to 45.8% in 2017-18.
    - ✓ The share of **workers who are eligible for social security benefits in non-agricultural sector** has increased from 45.5% in 2004-05 to 50.4% in 2017-18.

> **Conceptual Framework of Key Employment and Unemployment Indicators**
> - **Labour Force Participation Rate (LFPR):** It is defined as the percentage of persons in labour force (i.e. working or seeking or available for work) in the population.
> - **Worker Population Ratio (WPR):** It is defined as the percentage of employed persons in the population.
> - **Proportion Unemployed (PU):** It is defined as the percentage of persons unemployed in the population.
> - **Unemployment Rate (UR):** It is defined as the percentage of persons unemployed among the persons in the labour force.
> - **Activity Status**- The activity status of a person is determined on the basis of the activities pursued by the person during the specified reference period. It can be determined in two ways-
>   - **Usual Status:** When the activity status is determined on the basis of the reference period of **last 365 days preceding the date of survey**.
>   - **Current Weekly Status (CWS):** When the activity status is determined on the basis of a reference period of **last 7 days preceding the date of survey**.

  - **Rise in formal employment**- The share of workers employed in informal enterprises in industry and services, and non-crop producing agriculture, has dropped to 68.4% in 2017-18 from 72.5% in 2011-12.
  - **Workers moving away from agriculture**- into industry and services as **the share of workers engaged in the agricultural sector has declined** by about five percentage points, from 48.9% in 2011-12 to 44.1% in 2017-18.
  - **Technical/ Vocational Education**: 94.3% of those aged 15 or over in urban areas do not have technical education. The proportion of urban youth who received formal vocational training has improved to 4.4% in 2017-18.
  - **Income gap**: On average, a male employee earned nearly 1.2-1.3 times the earnings of female regular salaried worker in 2018. However, self-employed male workers earned 2 times more than the earnings of self-employed female workers in urban areas in 2018.

- According to the **Annual Public Enterprises Survey** (PES) series, the number of **casual and contract workers** has increased from 36% in 2014 to 53% in 2018.

Reasons for unemployment

- **Economic slowdown:** Currently, sectors like auto, real estate, banking, construction, agriculture and MSMEs - all of which contribute a considerable amount towards India's GDP - are facing a sharp demand slowdown.
- **Preference of voluntary unemployment:** Voluntary unemployment is preferred over low-paying jobs (especially when one paid high educational fees) i.e. adopting the 'wait-and-watch' policy for the right job profile and remuneration.
- **Downgrading of employment:** i.e. hiring of candidates, with higher but superfluous qualifications, for elementary positions (e.g. news reports of PhD holders applying for peon vacancies)
- **Lack of Industry- Academia cohesion:** Disparity between colleges'/universities' curriculums and industry requirements/ expectations.
- **Lack of vocational training:** which renders many unemployable.

Government Steps for employment generation

- MUDRA Bank Micro Units Development Refinance Agency (MUDRA) Bank
- Start Up India and Stand Up India Schemes
- Make in India Program
- The apparel and garments sector received a special package.
- Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA)

Way Forward on Job Creation

- **Shift development focus towards labour intensive sectors** to create more jobs, such as food processing, leather and footwear, wood manufacturers and furniture, textiles and apparel and garments.
- **Cluster development to support job creation** in micro, small and medium enterprises (MSMEs), with a specific focus on incentivizing these MSMEs to grow bigger to generate more jobs.
- **Formalisation of workforce:** where growth in jobs must be inclusive and new jobs need to be decent and secure with better work conditions including social security benefits and the right to organise.
  - Expansion of the organized sector to create well-paid high productivity jobs.
- **Greater focus** is required on **better and relevant skilling opportunities** so as to compete with neighbours and global competitors.
- **Expansion in export market by developing Coastal Employment Zones**, using better technology, and improving on quality to remain competitive.
- **Incentivizing industry:** Reducing corporate tax, easing lending norms and relaxing GST rules on a short-term basis are some of the reforms that could give companies more room for hiring and boosting productivity.
- The **public investments in health, education, police and judiciary** to create many government jobs.
- The government should introduce **reforms to quell the wage gap** and get more women to become a part of the country's workforce.
- India will have to **shed its service-led structure and transform into an innovation-driven economy** and focus on becoming a creator rather than an adopter.

Good jobs rather than number of jobs

- Often in the debate over the number of jobs required for India, a crucial aspect is missed i.e. India needs **good quality jobs** not merely large number of jobs.
- The NITI Aayog's **Three Year Action Agenda** also reported that **underemployment** is a more serious issue than unemployment. Experts have also suggested that **voluntary unemployment** could be a bigger headache for India in the coming years. It is strengthened by the following facts-
  - The **Consumer Pyramids Household Survey** quantifies the sharp fall in the rate of growth of jobs for the better educated in recent years. The data also suggests that the number of unemployed seeking jobs also decreased over time, implying that people are looking for **high-productivity, high-wage jobs.**
  - Similarly, many no longer want jobs and are turning into **entrepreneurs**.
- Thus, government policies need to focus on creating an enabling environment, which helps create such good jobs.

1.1.1. UNEMPLOYMENT DATA

Why in news?

Recently, the National Sample Survey Organisation (NSSO) released the Annual Report [July, 2017 – June 2018] and Quarterly Bulletin [October-December 2018] of the **Periodic Labour Force Survey (PLFS).**

Background

- There has been a debate over the **credibility of the data on unemployment figures** in India. Earlier, there were various sources to study employment and its composition such as-

<table>
<tr><th colspan="3">CLASSIFICATION OF SURVEYS AND STUDIES TO STUDY EMPLOYMENT AND ITS COMPOSITION IN INDIA</th></tr>
<tr><th>TYPE AND NAMES</th><th>DESCRIPTION</th><th>LIMITATIONS</th></tr>
<tr><td colspan="3">Household Surveys:
• (+) Comprehensively cover the entire labour force
• (-) These are conducted every five years
• (-) Time lag between data collection and availability of the results
• Eg. - Employment-Unemployment Survey (NSSO), Annual Labour Force Survey (Labour Bureau)</td></tr>
<tr><td colspan="3">Enterprise Surveys:
• (+) Better accuracy than Household surveys, in accessing industry structure, wages and other employment characteristics
• (-) Available sample frames may not cover small, unorganized enterprises
• (-) Self-employed and farm workers are excluded
• Eg. - Economic Census (by MOSPI), Annual Survey of Industries (MoSPI), Unorganized Sector Surveys of Industries and Services (NSSO), Quarterly Employment Survey (QES) (Labour Bureau)</td></tr>
<tr><td colspan="3">Social Security Schemes:
• (+) Wide coverage of new job additions
• (-) Highly partial coverage and potential double-counting of jobs
• (-) Substantial overlap across the government schemes
• Eg. - Employees' Provident Fund Organization (EPFO), Employees' State Insurance Corporation (ESIC)</td></tr>
<tr><td colspan="3">Other sources:
• Administrative data: it includes tax returns and filings, pension and medical insurance programs etc.
  ○ (+) Good measure of formal employment
  ○ (-) Partial coverage
  ○ (-) Difficult to gauge addition of jobs
• Data from government schemes: it includes estimates via MGNREGA, MUDRA, job creations under programs such as ICDS, PMKVY, DDUGKY etc.
• Emerging sources: GSTN, Big Data analytics</td></tr>
</table>

- The **available estimates were either out-dated or based on surveys with design flaws** that render them unsuitable for inferring nationwide employment level.
- Concurrently, the NSSO started an exercise named the **Periodic Labour Force Survey (PLFS)** that will provide annual estimates of labour force, employment, unemployment, industry structure of workforce, nature of employment and wages nationally and regionally on an annual basis. The PLFS replaces the NSSO's **Employment-Unemployment Survey.**

Changes introduced in the PLFS Survey

- It has **twin objectives**-
  - To measure **quarterly changes of various statistical indicators** of the labour market in **urban areas**. Households in urban areas were visited four times, constituting a rolling panel for 3 quarters. This facilitates analysis of the changes in seasonal employment and employment characteristics in urban areas.
  - To generate the **annual estimates of different labour force indicators** both in **rural and urban areas.**
- So, the **Quarterly Bulletin** contains key indicators for **urban areas only**, whereas the **Annual Report** contains the indicators for both **rural** and **urban areas.**
- **Criteria for stratification-** Rather than using monthly per capita expenditure of the household, PLFS uses **education levels** of members of the households.
- **Usage of technology-** by adapting the World Bank Computer Assisted Personal Interviewing (CAPI) solution platform with appropriate inputs and data collected in the field using Tablets.

- **Better training of Field Investigators (FI)/Field Officers (FO)**- for a uniform understanding to ensure correct implementation of concepts and definitions while collecting data.
- This survey has tried to overcome the **reasons for low credibility** of data related to unemployment in India. Apart from the frequency of data, it has incorporated some **new features** to address the same.

Way Forward

No single data source is complete by itself. These data sets need to be supplemented by data from other sources so as to collectively give a holistic picture of the overall employment market. The research community and academia should give additional insight to the labour market to the public at large.

1.1.2. SKILL INDIA MISSION

- The Skill India mission was launched in 2015 along with the creation of the new National Policy for Skill Development and Entrepreneurship.
- Under the mission, the previous target of training 150 million people by 2022 was raised to a goal of 400 million people by 2022.
- The "demand-driven, reward-based" **Pradhan Mantri Kaushal Vikas Yojana (PMKVY)** flagship scheme was set up to achieve these targets.

Need for Skill Development

- **High unemployment rates:** There is a **direct link between India's underskilled workforce and high unemployment rates**. According to NSSO Report 2011-12, only 2.3% of the total workforce in India had formal sector skill training.
- **Demographic dividend:** India is expected to have the largest workforce in the world by 2025. To utilize this demographic divedend effectively, skill development must take primacy.
- **Moving towards innovation:** As we aspire to become a knowledge-based economy, development of highly skilled human capital is the key to raise innovation quotient of the workforce.

Other recent government initiatives for Skill development

- **Indian Institute of Skills:** Approval given for the setting up of Indian Institute of Skills (IISs) at different locations across the country in Public Private Partnership (PPP) mode.
- **Global Skills Park:** It is an international skilling institute to provide students with international training methods in world class machinery, tools & equipment. The Asian Development Bank (ADB) has approved a $150 million loan to establish the **first Global Skills Park in Madhya Pradesh**.
- The Cabinet has approved the merger of National Council of Vocational Training (**NCVT**) and National Skill Development Agency (**NSDA**) into **National Council for Vocational Education and Training (NCVET)** for improving the outcome of the Skill India mission.

Issues with Skill Development in India

- **Poor accreditation process**- The Quality Council of India (QCI) has often compromised with the quality of accreditation and affiliation process.
  - For eg: It had not followed the prescribed National Council for Vocational Training norms with respect to building infrastructure, equipment, and faculty.
- **Multiplicity of norms, procedures, curricula, certification**- Policies and initiatives related to skill development are spread across nearly 20 ministries and hence lacks coherency and holistic approach.
  - Same applies to the state-level Skill Development Missions where convergence cannot be ensured without robust coordination and monitoring mechanism.
- **Inadequate funding and spending**- There was a drastic cut in the amount allocated to the Ministry of Skill Development and Entrepreneurship (MSDE) due to underutilization of funds allocated to it.
- **Reluctance of the industry** in providing a wage differential for skilled workers, leading to low absorption of skilled manpower
- **Poor Industry interface**- For instance, there are too many sector skill councils (industry bodies mandated to ensure that skill development efforts are in accordance with the actual needs of the industry), each

Performance of Skill India

- As on January 2019, about **37.32 lakh** candidates have been enrolled across the country.
- Over **10.09 lakh** people trained under Skill India Mission's Pradhan Mantri Kaushal Vikas Yojana (PMKVY) have got jobs, with Uttar Pradesh, Madhya Pradesh, Haryana, Rajasthan and Tamil Nadu reporting highest placements.

trying to maximise their business. Also there is no of credible assessment board to uphold the accountability of these sector skill councils.

- **Lack of integration with formal education** and lack of focus on outcomes.
- **Underutilized Capacity of the industrial training institutes**- The total trainee count in the ITIs is 19.4 lakh as against the seating capacity of 21.9 lakh.

Way Forward

- **Skill Voucher** to be redeemed by the institutions can be introduced as a **financing instrument.** They can be given to a beneficiary that enables them to sign up for vocational education course at any accredited training institute.
- **Industry should be incentivized** to set up training institutions in **PPP mode**, curriculum development, training modules, provision of equipment, training of trainers etc. The working of sector skill councils should be improved as recommended by the **Sharda Prasad Committee**.
- **Evaluation of Training Institutes:** There is an urgent need to provide quality training to the students to enhance their employability. In addition to providing grants to training institutes, NSDC should also develop some techniques to evaluate the performance of such institutes and encourage them to perform better.
- **Local bodies** can be **used for skill mapping** and creating a data base of youth at local level to assess demand supply gaps.
    - The **personnel of Railways and other para-military forces** could be used for skill training or lending institutional support in imparting training in hilly, inaccessible and difficult terrains.
- **Stronger facilitation support** to avail MUDRA loan should be provided to PMKVY certified candidates.

1.2. LABOUR REFORMS

Labour is a concurrent list subject, thus there is multiplicity of laws at Centre and the State levels. Amidst this, the focus of labour reforms should be twin-fold: to promote creation of formal sector jobs, and to not stifle employers by over-protection of workers.

Agenda for Labour Reforms

- **Consolidation and simplification** of numerous States' and Centre labour laws
- Streamlining of **Minimum Wages** in the country and ensuring they reach the beneficiaries.
- Introduction of **fixed term employment**, to curb tendency for employing (socially insecure) contract labour

1.2.1. CONSOLIDATION OF LABOUR LAWS

The 2nd National Commission of labour had recommended simplification, amalgamation and rationalisation of Central Labour Laws. The government has been working in that direction and has introduced for labour codes-

Proposed Code	Need for the code	Key Provisions
Labour Code on Wages Bill, 2019	• It arises in the absence of statutory National Minimum Wage for different regions, which impedes the economic prospect. • It seeks to **consolidate laws relating to wages by replacing**- Payment of Wages Act, 1936; Minimum Wages Act, 1948; Payment of Bonus Act, 1965 and Equal Remuneration Act, 1976	• The Code **will apply to any industry, trade, business, manufacturing or occupation** including government establishments. • Wages include salary, allowance, or any other component expressed in monetary terms. This will not include bonus payable to employees or any travelling allowance, among others. • **It differentiates the central and State Jurisdiction** in determining the wage related decision for establishment such as Railways Mines and oil fields. • A concept of statutory **National Minimum Wage** for different geographical areas has been introduced. It will ensure that no State Government fixes the minimum wage below the National Minimum Wages for that particular area as notified by the Central Government.
Labour Code on Industrial	• It aims **to create greater labour market flexibility and discipline in labour**	• It increases the employee limit from 100 to 300 above which, the government approval is needed for layoff/retrenchment/closure

Relations Bill 2015	– to improve upon ease of doing business and also to encourage entrepreneurs to engage in labour-intensive sectors. • It would **replace three laws** i.e. Trade Unions Act, 1926; Industrial Employment (Standing Orders) Act, 1946 and the Industrial Disputes Act, 1947.	– this provision has been criticized sharply by the labour groups and trade unions. • It provides that 10% of workers shall apply (be applicant) for registering a trade union – this has also invited opposition from various worker groups and trade unions. • For employers employing < 50 employees, the requirement to provide a minimum of 1 months' notice and retrenchment compensation (severance) is to be removed.
Labour Code on Social Security & Welfare, 2017	• **Almost 90% of the current workers are not covered under any social security.** • The current thresholds for wage and number of workers employed for a labour law to be applicable creates tenacious incentives for the employers to avoid joining the system which results in exclusions and distortions in the labour market.	• **Definition of employee and categorization of workers** covers all kinds of employment including part-time workers, casual workers, fixed term workers, piece rate/ commission rated workers, informal workers, home-based workers, domestic workers and seasonal workers. • A proper **percentage-based structure for contribution**, vis-à-vis socio economic category and minimum notified wage, has been put in place under the Code. • It **introduces new approaches to ensure a transparent and fair financial set up**, such as, ○ Time bound preparation of Accounts within six months of the end of the financial year; ○ Provision for social audit of social security schemes by State Boards after every five years; ○ Accounts of Intermediate Agencies to be subject to CAG Audit on the same lines as that of Social Security Organizations. • **Wage Ceiling and Income Threshold**: The term 'wage ceiling' is for the purpose of determining a maximum limit on contribution payable; whereas the term 'income threshold' is for the purpose of enabling the government to provide for two different kind of schemes (for same purpose) for two different class of workers. • **Contribution Augmentation Funds** would be established through which governments could contribute to the social security in respect of workers who are unable to pay contribution. • **National Stabilization Fund** will be used for harmonizing the Scheme Funds across the country and will be managed by the Central Boards.
Labour Code on Occupational Safety, Health & Working Conditions, 2018	• The proposed code is the first single legislation **prescribing standards for working conditions, health and safety of workers** and it **will apply on factories with at least 10 workers.** • It will **amalgamate 13 labour laws** including the Factories Act, 1948; the Mines Act, 1952; the Building and Other Construction Workers (Regulation of Employment and Conditions of Service) Act, 1996; the Contract Labour (Regulation and Abolition) Act, 1970 etc.	• Centre has been empowered to prescribe standards on occupational safety and health • **Annual health check** to be made mandatory in factories and its charge will be borne by the employers • **Appointment letters** for all workers (including those employed before this code), underlying their rights to statutory benefits • **At least 50% of penalty** levied on employers could go towards providing some relief to families of workers who die or are seriously injured while working • **National Occupational Safety and Health Advisory Board** at national level and similar bodies at state level, have been proposed to recommend standards on related matters. • **Appointment of facilitators** with prescribed jurisdiction for inspection, survey, measurement, examination or inquiry has been proposed • **Mandatory license** for every contractor who provides or intends to provide contract labour. Also, license is needed for industrial premises as well

		• Various allowances such as **journey allowance and displacement allowance** have been proposed for interstate migrant workers. • **Site Appraisal Committee** is proposed to be established by state government to examine applications for the establishment of a factory involving hazardous process and make its recommendation to the State Government

1.2.2. NATIONAL MINIMUM WAGE

Why in news?

- The Expert Committee under the Chairmanship of Dr. Anoop Satpathy has brought out a timely technical Report on "**Determining the Methodology for the Fixation of the National Minimum Wage (NMW)**".
- A uniform national minimum wage of Rs 9,750 per month or region-wise minimum wages ranging from Rs 8,892-Rs 11,622 per month for five regions (as of July 2018) has been recommended.

Background

- **The Payment of Wages Act, 1936, and the Minimum Wages Act 1948**, sought to provide protection and ensure better working conditions for low-paid workers
- The **absence of criteria** in the Minimum Wages Act to determine minimum wages has been addressed by **Indian Labour Conference and SC recommendations** providing guidelines for this purpose.
- Over the years, there has been a demand to improve the minimum wage policy and even an interest in framing a "national wage policy".
- In 2017, Code on Wages Bill, provided for bringing in a statutory National Minimum Wage. In this regard, this expert committee was tasked to determine the methodology for the same.

Minimum Wage
- It is the wage which is **paid by an employer/industry to its workers irrespective of its ability to pay.**
- It must provide not only for the bare sustenance of life, but for the preservation of the efficiency of the workers.

Living Wage
- It should enable the earner to provide for himself and his family not only the bare essentials of food, clothing and shelter but a measure of frugal comfort including education for his children, protection against ill-health, requirements of essential social needs and a measure of insurance against the more important misfortunes including old age.

Fair Wage
- It is **linked with the capacity of the industry to pay**.
- Factors such as labour productivity, prevailing wage rates, the level of national income and its distribution etc. are variables in determining fair wage.
- It is **above the minimum wage but below the living wage**.

Issues with Minimum Wage System in India

- **Issues relating to its coverage**- today, there are nearly 429 scheduled employments and 1,915 scheduled job categories for unskilled workers. This massive expansion in job categories and wage rates has led to major variations not only across states but also within states.
- **Lack of uniform criteria for fixing the minimum wage rate**: Some states link the wages to the cost of living through a variable dearness allowance (VDA) and some states do not.
- **Minimum Wages Act does not cover all wage workers**- as one in every three-wage workers in India is not protected by it.
- **Presence of gender discrimination**- For instance, women dominate in the category of domestic workers while men dominate in the category of security guards. While both these occupations fall within the category of unskilled workers, the minimum wage rate for domestic workers within a state is consistently lower than that for the minimum wage rates for security guards.
- **Compliance with the act**- It has also been observed that compliance levels are significantly higher for regular wageworkers when compared to casual wage earners.

Need of the National Minimum Wage

- **To ensure a uniform standard of living across the country**- At present, there are differences in minimum wages across states and regions as both the central and state governments set, revise and enforce minimum wages for the employments covered by them.
- **Allow for easier implementation and compliance with the minimum wage law-** as it will reduce ambiguity and confusion over multiple wage laws.

Recommendations of the Committee

> **International Conventions on Minimum Wages**
> - The ILO Minimum Wage Fixing Machinery Convention, 1928
> - Minimum Wage Fixing Machinery (Agriculture) Convention, 1951
> - Minimum Wage Fixing Convention, 1970

- **Need to update existing norms for fixing minimum wages**- in the light of the latest available evidence relating to per household consumption units, food and nutritional requirements, changing consumption pattern and non-food expenditure requirements.
- **Need for elaborating a nationally representative and culturally palatable food basket**- by adopting an approach that would focus on a balanced diet rather than merely its calorie intake. Hence, committee recommends minimum wage at a level that would allow for a minimum recommended intake (per adult person per day) of 2,400 calories, 50 grams of protein and 30 grams of fats.
- **Intermediate adjustment for inflation**- to accommodate changes in prices at least in every six months, on the basis of the CPI made available by the CSO.
- **Non-food items**- For estimating the required expenditure on non-food items, the committee identifies two groups of commodities:
    - **Essential non-food items**, namely clothing, fuel and light, house rent, education, medical, footwear, and transport;
    - **Other non-food items**, such as entertainment, durable goods, toilet articles, other household consumables, consumer services excluding conveyance, and consumer taxes
- **Single value of the National Minimum Wage**- for India should be set at Rs.375 per day as of July 2018. This would be equivalent to Rs.9, 750 per month, irrespective of sectors, skills, occupations and rural-urban locations.
    - It has also recommended to introduce an **additional house rent allowance** (city compensatory allowance), averaging up to INR 55 per day i.e., INR 1,430 per month for urban workers over and above the NMW.
- **Method for estimating the NMW at the regional level**- For the purpose of estimating national minimum wages at regional levels, the committee has grouped the **states into five regions** based on a composite index and have recommended region specific national minimum wages.
- **Minimum wages should be fixed at round numbers**-which are much easier to disseminate. This will also facilitate the minimum wage enforcement process.
- **Creation of a research unit in the Ministry of Labour and Employment**- to support the Central Advisory Board and State Advisory Boards at the time of formulating recommendations to set and adjust minimum wages.

1.2.3. FIXED-TERM EMPLOYMENT RULES

Why in news?

The Union Ministry of Labour has urged States to issue orders permitting fixed-term employment (FTE) across all industries.

> **What is fixed term employment?**
> - FTE is **a contract in which a company hires an employee for a specific period of time**.
> - The **employee is not on the payroll of the company**.
> - Their **payment is fixed in advance and is not altered till the term expires**.
> - Such contracts are given out for temporary jobs and not for routine jobs.
> - Such **workers are entitled to all statutory benefits** (work hours, wages etc.) available to a permanent worker in the same establishment. However, other benefits such as **Provident Fund is not available to them.**
> - The employers can terminate the contract on certain grounds (fraud, non-performance, etc.) even before the due date. The temporary worker having completed 3 months in service shall get 2 weeks' notice before termination.

Background

- **Industrial Employment (Standing Orders) Central (Amendment) Rules, 2018** in March notification **allowed all industries to hire workers on contract with a fixed tenure.**
- Since, **labour is a concurrent list subject** and without a Parliamentary ratification, States are not really obliged to follow these orders.
- In order to plug this gap, the Central Government has asked the states to issue separate notifications for the same.

Benefits of Fixed-Term Employment

- **Fixed wages and work conditions:** The workers are ensured to have a fixed wage and work conditions from before. This provides them livelihood security for the given period.

- **Accountability:** The workers are entitled to have statutory benefits. Therefore, they gain greater sense of accountability from the principal employer.
- **Forecast labour costs:** The fixed term contract enables the business to forecast their labour costs. It also provides relief against protests related to salary hikes etc.
- **Short term Employment shortage:** During peak seasons, industries face shortage of workers. Fixed-term employment will help them to hire and remove workers according to their requirements without extra legislative burdens.
- **Commercial Competitiveness**: Due to in-built flexibility in hiring and firing the workers, the business will be able to safeguard its commercial competitiveness through finding suitable employees.
- **Job Creation:** FTE is expected to boost job creation, provided the cost of capital does not remain so low as to deter labour use.

Criticism against the move

- **Hire-and-fire:** Central trade unions are protesting against the government's policy of hire-and-fire. Trade unions will go unrecognised by the move.
- **Removal of Safety nets:** as the government has enabled the employers to sidestep even the minimum protection offered by the Factories Act 1948, Industrial Disputes Act 1947 and Contract Labour (Regulation and Abolition) Act 1970.
- **Undermines Job Regularisation:** Collective bargaining talks for wage increase will not be possible. Business will have no incentive to regularise the jobs.
- **Against the earlier judgments of Supreme court:** The courts have allowed FTE only in seasonal activities. The Supreme Court has ruled earlier that a fixed-term contract worker who had worked for 7 years should be regularised.
- **Industries will be converted into Sweatshops:** The major reason of conflict of workers with management (e.g. in Maruti-Suzuki incident) is common issues of non-recognition of trade unions, temporary workers far outnumbering regular workers and paying them very low wages. The move may encourage the same.

What needs to be done?

- The FTE conditions need to be **defined clearly to make them acceptable to both employers and employees**.
  - The present rules are silent about the minimum or maximum term of an FTE and the maximum permissible number of consecutive FTEs.
- The norms should be arrived at in a **transparent, consensual manner**. Labor reforms will not be politically acceptable in the absence of a better social safety net.
- Since labour comes under Concurrent list, a suitable and well discussed legislation for FTE should come through Parliament.

2. INCLUSIVE GROWTH

Inclusive Growth

- The central idea of the inclusive growth includes **sharing of fruits of socio-economic development with all sections of the society**. Inclusive growth, sustainable development and poverty alleviation are intimately interlinked.
- India has been working towards inclusive growth through its welfare state approach since independence and it remained a policy focus of the successive governments and the **12th Five Year Plan** was even titled as – **"Faster, sustainable and more inclusive growth"**.
- Despite the higher growth rates achieved after the economic liberalization, the growth has not been equitable.
- An Oxfam report titled 'Reward Work, Not Wealth' highlighted that **the richest 1% in India cornered 73% of the wealth generated in the country** last year. Besides, 67 crore Indians comprising the poorest half saw their wealth rise by 1%.
- Numerous programmes associated with inclusive growth include: MGNREGA, IAY, NHRM, NSAP, SSA, JNNURM, NAPCC, Digital India, Skill India and so on.

2.1. FINANCIAL INCLUSION

2.1.1. PRADHAN MANTRI JAN DHAN YOJANA

Why in News?

The government decided to make the Pradhan Mantri Jan Dhan Yojana (PMJDY) an open-ended scheme, meaning that it will continue indefinitely.

New incentives

- The **overdraft facility has been doubled** from Rs. 5,000 to Rs. 10,000.
- There will be **no conditions attached for over-draft of up to Rs 2,000**. Also, the **upper age limit** for availing the facility **has been hiked** to 65 from the earlier 60 years.
- **Accidental insurance cover** for new RuPay Cardholders **has been raised** from Rs 1 lakh to Rs 2 lakh.

Pradhan Mantri Jan Dhan Yojana

- It is a **financial inclusion program** of Government of India that aims to expand and make affordable access to financial services such as bank accounts, remittances, credit, insurance and pensions.
- It focuses on **coverage of households** as against the earlier plan, which focused on coverage of villages. It focuses on **coverage of rural as well as urban areas.**
- The plan also envisages **channelling all Government benefits** to the beneficiary's accounts and pushing the Direct Benefits Transfer (DBT) scheme of the Union Government.

Significance

- Poor households in India, in the absence of access to formal credit, have to deal with moneylenders who charge exorbitant rates of interest. Household Survey on India's Citizen Environment and Consumer

Economy, 2016, shows that **within the poorest section of the population two in three take credit from informal sources.**

- Though access **to formal financial institutions** has improved over time but still thousands of villages not have a bank branch and **less than 10 percent of all commercial bank credit goes to rural area**.

Achievements

- **Helped in financial inclusion**- As per the Global Findex Database, almost 80% of adult Indians have bank accounts. Financial inclusion has taken place in three ways
    - **Financialisation of savings**- by giving lower income households access to a safe investment product.
    - **Diversification of financial products**- with 13.5 crore beneficiaries enrolling for the low-cost accident insurance cover and 5.5 crore for the life cover.
    - **Transition to electronic payments**- with 27.7 crore-account holders now having Rupay debit cards.
- **Helped banking sector**
    - **Improved balance sheets of banks**- even though they still make up less than 1 per cent of banks' deposit base, they sustained growth in a year when deposit flows were hard to come by.
    - **Falling percentage of zero balance accounts**- from 58% in 2015 to 15 % as on January 2019, with even the percentage of inoperative accounts declining from 19.8% in 2017 to 16.3% as on December 2018.
    - **Servicing Cost is not an issue for the banks now**- as the average deposit balance in these accounts has increased.
- **Helped in inclusive growth**
    - **Focus on rural India**- Of 35.70 crore account holders, those from rural & semi-urban regions are 21 crore.
    - **Women empowerment**- Around 18.88 crore account holders are women.
- **Direct benefit transfer**- data submitted by the government to Parliament shows that 23 per cent of these accounts received direct benefit transfers as on August 2018.
- **Plugging Leakages from Subsidy:** According to the **Economic Survey for 2015-16** leakages in LPG subsidy transfers **fell 24%** and the exclusion of beneficiaries had been greatly reduced, due to banking infrastructure created by the combination named as **JAM trinity.**

Challenges

- **Dependency on unsecured debt**- Access to bank accounts seems to have had little effect on the dependence on private moneylenders.
- **Internet connectivity issues**: The inadequate infrastructure base for internet facilities basically in tribal and hilly areas make it difficult for Business Correspondents to deliver the required basic banking services.
- **Funds for Overdraft Facility:** Clarity has still not emerged on where the funds would be diverted from to finance the overdraft facility.
- **Increasing Cost of Business Correspondents:** If these accounts have to be functional and not remain dormant then the density of banking correspondent has to be increased, which will increase the cost of delivering the banking services.
- **Tackling Unaccounted Money Deposited During Demonetisation:** After the announcement of Demonetization total deposits in 255 million Jan Dhan accounts have increased to Rs 642521 million by November 2016.

Way forward

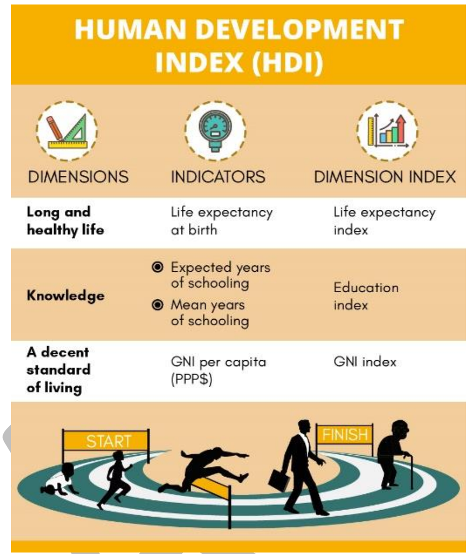
- With the high deposits in the banks, the **Government must nudge the banks to offer much-needed loan products** to the account holders. Allowing them to build up a credit and transaction history in the banking system is critical to wean them away from the grip of informal money lenders.
- The Centre and the RBI also need to make sure that the **first-time adopters are treated well at bank branches**, know the grievance redressal mechanisms and are aware of, and protected from, the consequences of fraud or misuse of their accounts.
- The policy focus should shift from the **quantity of inclusion to the quality of inclusion**. The measure of success of the scheme should include clearly-defined targets for usage and transactions.
- Launching **massive campaign programmes** among the poor households focusing on improving the level of **financial literacy and education** can help them recognize the benefits they can avail under the scheme and the responsibilities associated with it.
- It is recommended that **internet connectivity and speed should be increased** in tribal and hilly areas so that the ease of doing banking transactions can be entertained.

2.2. POVERTY AND HUMAN DEVELOPMENT

2.2.1. HUMAN DEVELOPMENT INDEX

Why in news?

India's ranking in UN's Human Development Index (HDI) went up by one from last year, to **130th among 189 countries,** released by the **United Nations Development Programme (UNDP).**



Facts on Index

- Within South Asia, India's HDI value is above the **average of 0.638 for the region,** with Bangladesh and Pakistan, countries with similar population size, being ranked 136 and 150, respectively.
- Between 1990 and 2017, **India's HDI** value increased from **0.427 to 0.640,** an increase of nearly 50 per cent and an indicator of the country's remarkable achievement in lifting millions of people out of poverty putting the country in **the medium human development category.**
- India's **life expectancy** increased from **57.9(1990) to 68.8(2017).**
- India's **per capita income** in **PPP** terms saw an increase of a 267% from **$1,733 to $6,353** between 1990 and 2017.
- **Expected years of schooling** went up from **7.6 years (1990) to 12.3 years (2017).**
- Development hasn't been spread evenly, with India's **income inequality the highest at 18.8%** – compared to 15.7% for Bangladesh and 11.6% for Pakistan. In fact, when corrected for **inequality India's HDI value falls by 26.8% to 0.468.**

Outcome for India

- Most of **the improvements have flowed to the top of the social pyramid** while those at the base have only just been lifted out of poverty.
- **Middle class hasn't grown** as much as it should have, while small and medium enterprises have failed to transfer the agrarian workforce to manufacturing.
- **Inequality remains a challenge for India** as it progresses economically.
- In India, **women remain significantly less politically, economically and socially empowered than men.** For instance, women hold only 11.6 percent of parliamentary seats, and only 39 percent of adult women have reached at least a secondary level of education as compared to 64 percent males.
- Female participation in the labour market is 27.2 percent compared to 78.8 percent for men.

Human Capital Index

- Recently, the first **Human Capital Index (HCI)** was released **by World Bank.** It measures the amount of human capital that a child born today can expect to attain by age 18. It **conveys the productivity of the next generation** of workers compared to a benchmark of complete education and full health.
- **Human Capital Index:** A child born in India today will be **44 % as productive** when she grows up as she could be if she enjoyed complete education and full health.
- **Probability of Survival to Age 5:** 96 out of 100 children born in India survive to age 5.
- **Expected Years of School**: In India, a child who starts school at age 4 can expect to complete 10.2 years of school by her 18th birthday.
- **Healthy Growth (Not Stunted Rate)**: 62 out of 100 children are not stunted. 38 out of 100 children are stunted, and so at risk of cognitive and physical limitations that can last a lifetime.

Suggestion in report to Improve Human Capital

- **Improving Social Investment:** Investing in human capital, particularly early childhood education, to develop high-order cognitive and socio-behavioral skills in addition to foundational skills.
- **Enhancing social protection:** A guaranteed social minimum (Universal basic income) and strengthened social insurance, complemented by reforms in labor market rules in some emerging economies is must for developing a just and equitable society.
- **Creating fiscal space** for public financing of human capital development and social protection by imposing property taxes in large cities, excise taxes on sugar or tobacco, carbon taxes etc. to increase a government's revenue.
- **Optimizing taxation policy** and improving tax administration to increase revenue by eliminating the tax avoidance techniques used by firms to increase their profits.

2.2.2. POVERTY AND SHARED PROSPERITY 2018

Why in news?

World Bank has released its report on global poverty **'Poverty and Shared Prosperity 2018: Piecing Together the Poverty Puzzle'** where it has advocated for some new measures of poverty.

Proposed New Measures of Poverty

To expand the understanding of poverty as a complex, multifaceted problem and identify pockets of people who are impoverished but have remained unnoticed, the World Bank has introduced **new measures of poverty**, which are-

- **New Poverty lines of US$3.20 and US$5.50 per person per day,** expressed in 2011 PPP. The value of these lines is derived from the typical poverty line in lower- and upper-middle-income countries, respectively. These higher-valued poverty lines reflect social assessments of what defines minimum basic needs in countries at these income levels in these countries.
- **The Societal Poverty Line (SPL)**- It is a combination of the absolute International Poverty Line (IPL) and a poverty line that is relative to the median income level of each country. It reflects how monetary definitions of poverty at the national level vary with the overall income in a society.
- **Individual Level of poverty**- looking into intra-household inequality among various age-groups and gender. The common approach assigns all individuals within a household to the same poverty status as the household. However, this masks potential differences in poverty among household members. This measure overcomes this.

Poverty Measurement in India

Studies conducted in India to define poverty and fix a poverty line:

- **Working Group Poverty Line** (1962): it took a household of five members as a unit; the line was fixed at INR 20 per capita (at 1960-61 prices).
- **Task Force Poverty Line (1979) under Dr. Y K Alagh**: It defined the poverty line as per capita consumption expenditure level, which meets the average per capita daily calorie requirement of 2400 kcal in rural areas and 2100 kcal in urban areas **along with the associated quantum of expenditure on non-food items** such as clothing, shelter, transport, education, health care, etc.
- **Expert Group (1993) under Prof. D T Lakdawala**: It disaggregated the national level rural and urban poverty lines as defined by the Task Force (1979) into state-specific poverty lines.
- **Expert Group (2009) under Prof. Suresh Tendulkar:** It advocated the use of Mixed Reference Period (MRP) based estimates of consumption expenditure as the basis for future poverty lines as against the previous practice of using Uniform reference period (URP) estimates of consumption expenditure.
- **Expert Group (2012) under Dr. C. Rangarajan**: It provides an alternate method to estimate poverty levels and examine whether poverty lines should be fixed solely in terms of a consumption basket and purchasing power parity.
- **NITI Aayog Task Force**: NITI AAYOG also proposed four options to arrive at a poverty line with due considerations from other stakeholders. Other highlights:
    - Track progress over time of the bottom 30% of the population.
    - Track progress along specific components of poverty such as nutrition, housing, drinking water, sanitation, electricity and connectivity.
    - NITI Aayog favoured the Tendulkar line, which set poverty ratio to 21.9 % as compared to Rangarajan committee, which had a higher poverty ratio of 29.5%.
    - To remove any criticism that many poor would be left behind if poverty line as per Tendulkar committee is adopted, NITI Aayog has underlined that it will only be used to track progress in combating poverty rather than identifying the poor for entitlements.
    - SECC data as suggested by Saxena and Hashim committee will be used for entitlements.
- **Various points of criticism against the above approaches include**- Inappropriate adjustment procedure for consumption levels, Use and uniform application of WPI as a deflator to represent price change in the poverty line, Use of fixed consumption basket over time, Debates on recall periods.

2.2.3. MULTIDIMENSIONAL POVERTY INDEX-2018

Why in news?

The 2018 global Multidimensional Poverty Index was released by the United Nations Development Programme (UNDP) and the Oxford Poverty and Human Development Initiative (OPHI).

Key findings of MPI 2018

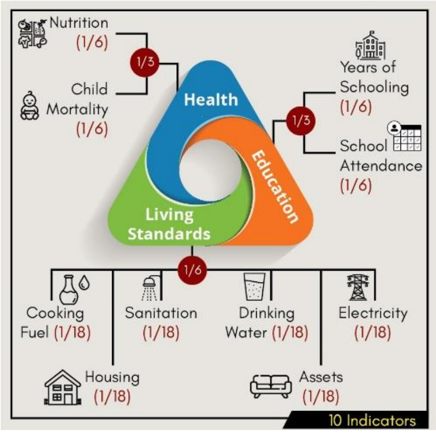
The global Multidimensional Poverty Index (MPI)-2018 covers 105 countries in total, which are home to 75 per cent of the world's population, or 5.7 billion people.

- A total of **1.34 billion people from 105 countries are multidimensionally poor** i.e. 23.3% of the people living in these countries.
- Multidimensional poverty is much **more intense in rural areas than urban areas;** globally there are 1.1 billion people living in multidimensional poverty in rural areas, compared to 0.2 billion people living in multidimensional poverty in urban areas.
- **In India,** 271 million people moved out of poverty between 2005-06 and 2015-16, but the country still has the **largest number of people living in multidimensional poverty in the world** (364 million people). Even so, India has cut its poverty rate from 55% to 28% in ten years.

The MPI measures
- **Incidence of poverty:** the proportion of the population who are poor according to the MPI.
- **Average intensity of poverty:** the average share of deprivations people experience at the same time.
- **MPI value:** The MPI value, which ranges from zero to one, is calculated by multiplying the incidence of poverty by the average intensity of poverty. It shows the proportion of deprivations that a countries' poor people experience out of the total possible deprivations that would be experienced if every person in the society were poor and deprived in every indicator.

A **person is identified as multidimensionally poor (or 'MPI poor') if deprived in at least one third of the dimensions.**

3 Dimensions of Poverty



How MPI is better than Income Poverty?

- As per World Bank, **international poverty line is currently valued at $1.90** in terms of 2011 purchasing power parity. Income allows people to meet basic needs but at a practical level income does not always provide a sufficient representation of poverty.
- From this perspective, income is the means to ends, while the ends themselves are the satisfaction of basic human needs. The multidimensional approach has a direct focus on the ends.

What's new in MPI-2018?

The new global MPI has changes in five of the ten indicators from the original MPI: nutrition, child mortality, and years of schooling, housing and assets.

- The **new threshold for nutrition** includes BMI (Body Mass Index)-for-age, and stunting as well as underweight for children.
- **For child mortality**, it considers whether a child has perished in the household in the last five years preceding the interview date.
- For **years of schooling**, the new threshold requires six years, rather than five years, of schooling.
- A household is deprived in the **housing indicator** if the floor is made of natural materials; or the roof or walls are made of natural or rudimentary materials.
- Finally, the **assets indicator** now includes ownership of computers and animal carts.

MPI 2018 have been revised to better align with the SDGs. The MPI shows how deprivations related to SDGs 1,2,3,4,6,7, and 11 are concretely interlinked in poor people's lives.

- Since people are MPI poor if they are deprived in one-third of the weighted indicators, the MPI focuses on people who are being left behind in multiple SDGs at the same time.

Limitations of the MPI

- The indicators **include both outputs**, such as years of schooling, and **inputs**, such as cooking fuel. It also includes both **stock and flow indicators**. A stock indicator is measured at a particular point in time, and it may have accumulated in the past. On the contrary, a flow indicator is measured per unit of time. Surveys do not have flow indicators for all dimensions.
- Although the MPI indicators were selected in order to guarantee as much cross-country comparability as possible, **indicators' comparability is still imperfect** for two reasons.
  - In the case of nutrition, the information differs across the surveys used.
  - Even when they collect the same information, the minimum acceptable standards on certain indicators, such as some of the living standard ones, may vary greatly according to the culture.
- While the MPI goes well beyond a headcount ratio to include the intensity of poverty experienced, it does **not measure the depth of poverty**—how far away, on average, from the deprivation cut-off in each indicator poor people are. Nor does it measure inequality among the poor—how deprivation is distributed among the poor.

Why are there such wide discrepancies between MPI poverty estimates and $1.90/day poverty estimates in so many countries?

- The MPI complements income poverty measures. It measures various deprivations directly.
- In practice, **although there is a clear overall relationship** between MPI and $1.90/day poverty, **the estimates do differ** for many countries.
- **Possibilities can include public services, as well as different abilities to convert income into outcomes** such as good nutrition.
- The fact that there are differences does not mean that the national poverty number, or the MPI headcount is wrong – **these simply measure different conceptions of poverty.**
- At the same time, just as national poverty measures, in contrast, are designed to reflect the national situation more accurately and often differ in very useful ways from the $1.90 measure, some countries may wish to build a national multidimensional poverty index that is tailored to their context, to complement the global MPI.
- The relationship between these measures, as well as their policy implications and methodological improvement, are priorities for further research.

2.3. SOCIAL SECURITY

2.3.1. MINIMUM BASIC INCOME

Why in news?

Recently, there have been calls for introduction of Minimum Basic Income (MBI) in the country.

Concept of Minimum Basic Income (MBI)

The Minimum Basic Income is a **social welfare system** that guarantees a basic income to households, provided they meet certain conditions. This is **different from Universal Basic Income** (UBI) scheme, which is a periodic, unconditional cash transfer to all citizens on individual basis, without means-test or work requirement. To that extent, the Minimum Basic Income is a **conditional UBI or a quasi UBI (targeted).**

Income Support: National Examples

- **Madhya Pradesh Unconditional Cash Transfers Project**, more than 6000 beneficiaries were given income support besides existing subsidies.

International Examples

- Under **Finland's "Perustulokokeilu"** (Basic Income Experiment), unconditional income support was provided to the selected pool of unemployed people between 25 & 58.
- Brazil has an 'anti-poverty' programme called **'Bolsa Familia'**, involving a cash grant to families below a certain income level, provided they meet conditions such as overseeing their children's school attendance.

What are merits of the idea?

- **Social Justice & Equity:** There is a need for such ways to ensure a just society that needs to provide every individual a minimum income to provide for basic necessities.
- **Freedom of choice:** The poor in India are treated as subjects of Government's welfare policies, rather than economic decision makers. MBI treats them as agents and entrusts them with the responsibility of using welfare spending as they see best.
- **Poverty alleviation:** According to Economic Survey (2016-17), income transfers can reduce poverty to 0.5% at a cost of about 4% to 5% of the GDP, if those in the top 25% income bracket are not included.
- **MBI has potential to reduce rural distress** for e.g. it can decrease long term rural indebtedness, as propensity to save increases.
- **Better social development:** Pilot studies in Madhya Pradesh have shown that the income supplements can improve nutrient intake, school enrolment and attendance of female students, toilet building etc.
- **Financial Inclusion:** by augmenting rural income & promoting usage of bank accounts.
- **Other advantages** include administrative efficiency, gender equity (by taking individuals and not household as beneficiaries), insurance against shocks and flexibility in labor market.

Challenges

- **Definition of basic income:** It is difficult to reach on a consensus-based definition of 'Basic Income', which will be sufficient to meet basic needs. Tendulkar Committee poverty line of 33/- a day works out basic income of 12,000/- a year. It will cost 11-12% of GDP, in comparison to the existing subsidy burden of 4-4.5% of GDP.
- **Fiscal challenges:** Total fiscal cost will depend on 2 factors: (i) Coverage of the scheme (ii) Extent of substitution with existing subsides/schemes. Further there are various challenges like difficulty in exiting

subsidies, hostility in extracting more tax revenue from wealthy, medium term fiscal risk, and rising consumption may stroke inflationary pressure.

- **Cash vs Kind Dilemma:** While giving income support, it is assumed that the beneficiaries would be wise in their discretion. However, it suffers from challenges like misuse of cash (on demerit or sin goods), **increasing vulnerability of women and child** as finances of families are controlled by men, direct monetary benefits **not being inflation proof**, etc.
- **Targeted vs universal:** Universalisation is the key to efficient delivery of services against targeting proposed by these cash transfer schemes. Strict targeting may have its own problems like issues related to identification of beneficiaries. This needs an easily identifiable objective criterion. Otherwise, it cannot be claimed to be superior in terms of the leakages.
- **Basic income is no substitute for state capacity:** In developed countries, the cash transfers supplement existing social security provisions and are a top-up over and above universal provision of health & education. In the Indian context, most arguments in favour of MBI are premised on the inefficiencies of existing social security interventions and seek to replace them with direct cash transfers.
  - Cash transfers seek to create demand for services without supplying the services, which leaves the poor to depend on private service providers. The privatisation of basic services such as health and education may lead to the problem of accessibility (e.g. in remote areas) and large scale exclusion of the poor and marginalised.
- **Reduce worker productivity** and reduce incentive for skill development and increasing employability through constant effort.
- **Implementation Challenges:** The success of cash transfers depend upon the outreach of banking system & last mile connectivity

2.3.2. INSURANCE SECTOR IN INDIA

Why in News?

India's **insurance gap has widened despite deeper penetration** according to report **"A world at risk- Closing the insurance gap"** by Lloyd's of London.

- **Insurance gap:** It is a measure of the total value of assets divided by the value of assets that are protected by an insurance cover.
- **Insurance penetration**: It is the ratio of the total premium underwritten in a particular year to the GDP of the country or industry. It was 3.49% in 2016-17.
- 'Penetration' states the value of total premiums in relation to GDP, while 'Gap' measures the total cost not covered by insurance policies.

Insurance Sector in India

- In India, **the insurance gap** has widened from \$19.7 billion in 2012 to **\$27 billion in 2018**, even though non-life **insurance penetration** has improved marginally from 0.7 per cent of Gross Domestic Product (GDP) in 2012 to **0.9 per cent as of 2018**.
- **India currently accounts for less than 1.5 per cent of the world's total insurance premiums** and about 2 per cent of the world's life insurance premiums despite being the second most populous nation.
- India's life insurance sector is the biggest in the world with about 360 million policies which are expected to increase at a Compound Annual Growth Rate (CAGR) of 12-15 per cent over the next five years.
- The insurance industry plans to hike penetration levels to five per cent by 2020.
- India had also increased FDI limit to 49 per cent from 26 per cent in insurance sector to increase the investments in insurance.

Role of Insurance

- **Provide safety and security**: Insurance provide financial support and reduce uncertainties in business and human life. Insurance facilitates spreading of risk from the insured to the insurer
- **Generates financial resources**: It generate funds by collecting premium which are further invested in government securities and stock. It also helps in providing Employment opportunities leading to capital formation.
- **Promotes economic growth**: It generates significant impact on the economy by mobilizing domestic savings. It provides capital into productive investments especially for long-term investment needs. It enables to mitigate loss, financial stability and promotes trade and commerce activities those results into economic growth and development.
- **Spread of financial services in rural areas:** IRDA Regulations provide certain minimum business to be done in rural areas, in the socially weaker sections.

Challenges in Insurance Sector

- **Low Awareness:** A large majority of people in India believe that health insurance is not a worthy investment and therefore, avoid buying such insurance products.
- **Poor Distribution:** Distribution outside large cities is poor. There are large parts of the country where access to general insurance is limited. The reason insurers and distributors do not build a presence in small towns is that it is unviable.
- **Fewer product innovations:** While many essential products to mitigate risk are available, there are gaps in the insurance product portfolio that leaves large risks uninsured.
- **Pricing:** Insurers have been focusing on growing sales even if that creates a distortion in pricing for individuals.
- **Perception by influencers**: Another major challenge is posed by the media and influencers. Often, the life insurance industry is portrayed in a negative manner and hence the consumers become skeptical of the life insurance industry.

Govt's Initiatives for Insurance

- **National Health Protection Scheme** launched under Ayushman Bharat to provide coverage of up to Rs 500,000 to more than 100 million vulnerable families for secondary and tertiary care hospitalization.
- **Pradhan Mantri Jeevan Jyoti Bima Yojana (PMJJBY) and Pradhan Mantri Suraksha Bima Yojana (PMSBY)** to cover all poor households will bring the security of insurance benefits to the marginalised sections, giving basic economic protection in cases of death or injury through accidents of a family member.
- **Prime Minister Jan Dhan Yojana (PMJDY)** proposes to bring 60-crore basic accounts within its fold and providing services of micro insurance and unorganised sector pension schemes through these accounts, which will further bolster the economic security of lower income groups.
- **Pradhan Mantri Fasal Bima Yojana (PMFBY)** provides crop insurance to farmers against any losses to their crops.

Way forward

- **Promote Awareness:** It is necessary to promote more awareness among public about benefits of insurance through videos, social media, ads, organizing campaigns etc.
- **Multiple Channels of Distribution:** Linking insurance with allied finance products like housing loan, mutual fund investment, banks credit cards etc are the new channels for life insurance.
- **Huge Untapped Market**: The demographics and macro-economic factors in India are diverse and insurance systems have to be aligned to other programmes in the country in order to target every section.
- **Better regulation**: Regulatory policies can be made to ensure that insurance companies focus more on insurance targets than profitability.
- **Use of Technology:** Stakeholders will have to leverage Internet and other technology options to provide single window service so as to cross-sell and retain customers.

2.4. CIRCULAR ECONOMY

Why in news?

Recently at Circular Economy Symposium 2019, NITI Aayog CEO said that Circular Economy has the potential to generate 1.4 crore jobs in next 5-7 years.

What is Circular Economy?

- The circular economy is a **model of production and consumption, which involves sharing, leasing, reusing, repairing, refurbishing and recycling existing materials** and products as long as possible. In this way, the life cycle of products is extended.
- This is a departure from the traditional, linear economic model, which is based on a take-make-consume-throw away pattern.
- It relies on large quantities of cheap, easily accessible materials and energy.

Barriers to the implementation of a Circular Economy Model

- **Economic Barriers**:
  - **Social and environmental externalities** are not considered in prices;
  - Prices of raw materials are fickle and at low prices alternative, good quality secondary resources are not competitive;
  - These models are **harder to develop**, as most investors are still working under a linear economy logic.
  - Lack of **qualified professionals** with technical or ICT knowledge.
- **Institutional Barriers**:
  - Many companies still have goals that **focus on short-term value creation**, whereas the circular economy model is a long-term value creation model.
  - The GDP index **doesn't consider social and environmental externalities**, discouraging the creation of value in both these areas.

Need for a Circular Economy

- **Rise in consumerism**: The rise in consumerism has led to more frequent replacement of assets on account of increased spending power and economies of scale.
- **High resource demand**: At the current rate of growth of the economy, India's resource requirements are projected to be nearly 15 billion tonnes by 2030. Therefore, there is an urgent need for decoupling economic growth from resources, which can be achieved through a circular economy approach.
- **Import dependence**: India's dependence on the international market for accessing critical resources like rare earth minerals etc. due to shrinking reserves, technical constraints etc.
- **Waste creation:** The traditional linear economy approach results in massive waste generation at all stages of a product life cycle.

Benefits of a Circular Economy

- **Fewer Greenhouse Gas Emissions**: As a circular economy uses renewable energy, it could halve carbon dioxide emissions by 2030, relative to today's levels.
- **Fewer Negative Externalities** – Following the circular economy's principles, negative externalities such as land use, soil, water and air pollution are better managed, as well as the emission of toxic substances and climate change.
- **Increased Potential for Economic Growth**: The increase in revenues from new circular activities, together with a cheaper production by getting products and materials more functional and easily disassembled and reused, has the power to increase GDP.
- **Employment Growth** – According to the 'World Economic Forum ', the development of a circular economy model, can bring greater local employment in entry-level and semiskilled jobs. New job will be created through increases in:
  - Recycling and repairing practices,
  - An increase in new businesses due to innovation processes and new business models
- **Volatility Reduction and Safeguarded Supplies**: More recycled inputs would be used, leaving companies less dependent on the volatility of the price of raw materials.

Way Ahead

- **Need for Legislation to** promote the circular economy in the country. Several countries have recognised the centrality of the circularity as the new paradigm for sustainable development.
- Policies like **Zero Effect, Zero Defect in manufacturing stage, National Electricity Mobility Mission Plan** in consumption stage, and the various Waste Management Rules in disposal stage, if tweaked properly, can be the ideal for integrating circular economy into the fabric of the Indian economy.
- Ensuring the transition to circular economy call for **extensive collaborative efforts between key stakeholders**, including regulators, policy makers, corporates, and financial institutions would need to work to adopt circular business models.
- **Adequate financing needed** for realization of these newer opportunities through innovative financing instruments, such as Green bonds, municipal bonds, SDG-aligned bonds.

2.5. BLUE ECONOMY

Why in news?

Recently Sustainable Blue Economy conference was organized in Nairobi, Kenya.

About Blue Economy

- As per the World Bank, Blue Economy is **the sustainable use of ocean resources for economic growth**, improved livelihoods, and jobs while preserving the health of ocean ecosystem.
- It **covers several sectors linked directly or indirectly to the oceans** such as fishing, minerals, shipping and port infrastructure, marine biotechnology, marine renewable energy, marine tourism, ocean governance and education.

Importance of Blue economy

- **Economic:**
  - Oceans provide 30 percent of oil and gas resources.
  - 90% of goods trade takes place through Oceans Sea of Line Communication.

- Ocean contributes $2.5 trillion to world economy with around 60 million people are employed in fisheries and aquaculture.
- Seabed Mining of polymetallic nodules and polymetallic sulphides to extract nickel, cobalt, manganese and rare earth metals.

- **Environmental:**
  - Mangroves and other vegetated ocean habitats sequester 25 percent of the extra CO_2 from fossil fuels, i.e., Blue Carbon.
  - Protection of coastal communities from disasters like floods and storms.
  - A Sustainable Blue Economy can help to achieve commitments under UN's Sustainable Development Goals 2030, Paris climate agreement 2015 and the UN Ocean Conference 2017.

India as a Blue Economy

India is trying to achieve the potential of Blue Economy by promoting the spirit of **'SAGAR-Security and Growth for All in the Region'** in Indian Ocean Region. Some initiatives by India are:

- **Sagarmala Project**: Sagarmala initiative focus on three pillars of development
  - **Supporting and enabling Port-led Development** through appropriate policy and institutional interventions.
  - **Port Infrastructure Enhancement**, including modernization and setting up of new ports.
  - **Efficient Evacuation to and from hinterland** by developing new lines/linkages for transport (including roads, rail, inland waterways and coastal routes).
- **Coastal Economic Zones**: 14 CEZs are being developed under Sagarmala initiative covering all the Maritime States.
  - CEZs are spatial economic regions comprising of a group of coastal districts or districts with a strong linkage to the ports in that region.
  - CEZ will help to tap synergies of planned economic corridors.
- **Resource exploration**: India in recent times has shifted its focus towards Indian Ocean resource exploration. E.g. India has explored 75000 sq km of Indian Ocean Seabed and is developing technologies (like remotely operated vehicles) for mining the resources
- **International relations and security**: India is cooperating with Indian Ocean littoral countries and projecting itself as 'net security provider' to ensure a safe, secure and stable Indian Ocean Region (IOR). India is also cooperating with extra regional powers like US, Japan in IOR. E.g. Asia-Africa growth corridor, QUAD etc.

Challenges to Blue Economy

- **Unsustainable development near marine areas**: Physical alterations and destruction of marine and coastal habitats & landscapes largely due to coastal development, deforestation, & mining.
  - FAO estimates that approximately 57 percent of fish stocks are fully exploited and another 30 percent are over-exploited, depleted, or recovering.
- **Impacts of climate change:** Threats of both slow-onset events like sea-level rise and more intense and frequent weather events like cyclones. Long-term climate change impacts on ocean systems like changes in sea temperature, acidity, and major oceanic currents.
- **Geopolitical issues:** Geopolitical tussle between in various regions like South China Sea, Indian Ocean Region etc. and undermining International Laws like UNCLOS limits the countries from achieving the full potential of Blue Economy.
- **Unfair trade practices:** Many times fishing agreements allow access to an EEZ of country to foreign operators. These operators restrict transfer of specific fishing knowledge to national stakeholders leading to low appropriation of fisheries export revenues by national operators. So the potential for national exploitation of those resources is reduced in the long run.
- **Other non-conventional threats**: Defense and security related threats like piracy and terrorism combined with natural disasters (Small Island Developing States are particularly vulnerable).

Way Forward

- National investments must be complemented by regional and global cooperation around shared priorities and objectives. Instruments like blue bonds, insurance etc. can be explored.
- **Capacity development** of coastal communities in form of training and skill development in sustainable use of ocean resources, modern fishing techniques and coastal tourism
- **Anticipating and adapting to the impacts of climate change** is an essential component of a blue economy approach.
- The **effective implementation of the UNCLOS** is a necessary aspect of promoting the blue economy concept worldwide. The convention sets out the legal framework within which all activities in the oceans and seas must be carried out, including the conservation and sustainable use of the oceans and their resources.

3. FISCAL POLICY AND RELATED NEWS

3.1. FISCAL POLICY

3.1.1. INDEPENDENT FISCAL COUNCIL

Why in news?

15th Finance Commission's Chairman NK Singh has pitched for an institutional mechanism like a 'Fiscal Council' to enforce fiscal rules and keep a check on the Centre's fiscal consolidation.

Issues in fiscal management

- **Poor Budgetary Forecasting:** Budgets often **overstate revenue projections** (15 out of 20 years since fiscal 1998) and **understate expenditures** (12 out of 20 years since fiscal 1998). According to CAG Report in 2017, the **over-ambitious revenue targets** combined with the **lack of transparency in tax administration** lead overzealous taxmen resorting to 'irregular' and 'unwarranted' methods to meet targets.
- **Limited Tax Buoyancy:** Faster growth in nominal gross domestic product (GDP) usually leads to faster growth in tax collections. However, in India, **tax buoyancy shows no stable pattern** and hence, forecasting tax revenues is difficult.
- **Creative Accounting:** Moreover**, fiscal deficits are also understated** by the use of 'creative accounting' such as 'rolling over' a part of the overall subsidy bill & dues to the states to the next financial year; using PSEs like LIC to purchase divested stakes in the disinvestment process.
  - Such "creative" accounting has led to a decline in the headline fiscal deficit number but **failed to reduce India's public debt to GDP ratio**, adversely impacting India's macroeconomic stability.
- **Use of Extra Budgetary Resources (EBR):** Over the years, the Govt's **reliance on EBRs**- such as funds of state-owned enterprises like LIC, SBI etc - to fund Govt. programmes has increased, but it doesn't appear in real time fiscal deficit numbers. E.g. 61.4% of all capital expenditure outlined in the 2018-19 Budget is to be financed through EBR, up from 54% in 2016-17.
- **Absence of uniform fiscal consolidation rules for centre & states:**
  - Various cesses and surcharges, in which States' have no share, are becoming a disproportionate portion of overall divisible revenue. This is against the spirit of fiscal federalism and financial devolution process.
  - For State Govt., Art 293(3) provides a constitutional check over market borrowings while no such restriction is there for the centre.
  - States have constraints in managing their finances as the RBI controls their deficit and cannot float a bond on a state's behalf without the Centre's approval.
- **Non-adherence to Fiscal Responsibility and Budget Management (FRBM) Act targets:** Since 2003 FRBM law came into effect, there have been four pauses in the deficit targets enshrined in it and many occasions where the targets have been flouted.
- **Fiscal Populism:** Political class has the tendency to make fiscal policy over-expansive, which increases burden on future government and thus, has detrimental long-run impacts e.g. loan waivers to farmers, tax waiver to MSMEs etc.
- **Poor institutional infrastructure for monitoring:** CAG has presented its audit report on Compliance of the Fiscal Responsibility and Budget Management (FRBM) Act, 2003 but the assessment is only post-facto.

Why fiscal discipline is important?

- **To improve investment:** Pile-up of past domestic debt severely restricts the ability to finance new investment. If debt becomes unsustainable, there is an increased risk of default & hence, downgrading of sovereign credit ratings.
- **Increasing credit availability to private sector:** As more money is lent to government rather than invested in the market, corporate sector is crowded out leading to slower industrial and capital asset growth and potential loss of employment.
- **Control inflation:** Too much of government debt can lead to inflation and reduction in real interest rates. It might prompt people to invest more in gold and real estate, thereby accentuating the problem of poor economic liquidity and black money.

- **Intergenerational parity** will be hurt as future generations will have to pay increased taxes to settle the government debt.
- **Constitutional Requirement:** Article 292 of the Constitution envisages fiscal responsibility in the form of legislation that obliges the government to have a ceiling on debt.

Functions of Independent Fiscal Council

- Prepare **multi-year fiscal forecasts** for the central and state governments.
- Define a **sustainable level of public debt.**
- Provide an independent assessment of the central government's borrowing & fiscal performance.
- Government must also **consult the council** before **flouting fiscal deficit targets.**

Advantages of an Independent Fiscal Council (IFC)

- IFC's evaluation of budget announcements & forecasts would indicate how realistic government projections are. This would be a **check on competitive populism** in Indian polity and would **increase financial accountability of the government** to the Parliament.
- An institutional mechanism for sound fiscal practices will bring in **transparency**, **instill confidence among domestic & foreign investors** and improve policy outcomes.
- It will **promote the culture of proper disclosures** and good accounting practices within the Govt.
- Most fiscal councils across the world are able to **discipline lawmakers through 'comply or explain' obligations**— requiring governments to at least explain the divergence from the fiscal council's views.
- International experience suggests that a fiscal council improves the quality of debate on public finance, and that, in turn, helps build **public opinion favourable to fiscal discipline.**
- An institutionalized fiscal council would **enhance cooperation** with Finance Commission and GST Council.

Conclusion

According to International Monetary Fund (IMF), IFCs are now an indispensable part in the design of fiscal frameworks aimed at guiding fiscal policymakers' discretion. An independent fiscal council can bring about much needed transparency and accountability in fiscal processes across the federal polity.

3.1.2. INDIAN STATISTICAL SYSTEM

Why in news?

Recently, there have been controversies and debates over the **credibility of data and statistics** published by different agencies including government bodies, independent think tanks and private players.

Major statistics in India

Agency	Statistics
Central Statistics Office (CSO)	GDP, Index of Industrial Production, Energy Statistics, Infrastructure Statistics, National Income Accounting, Conduct of Annual Survey of Industries, Consumer Price Indices for Urban Non-Manual Employees, Human Development Statistics, Gender Statistics, Imparting training in Official Statistics.
National Sample Survey Office (NSSO)	Primarily data are collected through nation-wide household surveys on various socio-economic subjects, Annual Survey of Industries (ASI). Also collects data on rural and urban prices, crop statistics.

About Statistical Architecture in India

- India's modern statistical system took shape even before independence under the leadership of **Prof PC Mahalanobis** who was known as **'father of Indian Statistical System'**.
- The **Ministry of Statistics & Programme Implementation** (MoSPI) was later created in **1999** and the **National Statistical Commission** (NSC) was set up in **2005** in order to oversee the entire range of official statistics.
  - The Ministry has **two wings**, one relating to **Statistics** and the other **Programme Implementation.** The Statistics Wing called the National Statistical Office (NSO) consists of the **Central Statistical Office (CSO)** and the **National Sample Survey Office (NSSO).**
- Although, India has the history of producing credible economic statistics, but recently a group of **108 economists and social scientists** called for restoration of "**institutional independence**" and integrity to the statistical organisations in India freeing critical data releases from '**political interference.**'

General Issues with Indian Statistics

- **Data sources are not available readily**- e.g. Agricultural prices are based on mandis or retail touch-points, where such data may not be final and there are changes after the data is released.
- **Non-availability of critical fiscal data such as the data on pay and allowances.**
- **Capacity Building**- the human and organisational resources of the statistical agencies have not improved since the 1980s. The internal architecture needs a revamp to adapt to the changing data needs and data handling procedures.
- **Divergence in definitions and criteria**- of different indicators, which are used by various agencies.
- **Large unorganised Sector**- makes it problematic to get accurate data and a large number of proxies are used to arrive at output numbers.
- **Lack of transparency and reliability of fiscal data due to cash-based accounting.**
- **Lack of continuous long-term series of fiscal data**- e.g. Trade data is based on how the reporting is done, and while the RBI-BOP data is straightforward as it looks at entry and exit of forex from the system in a particular time period, the data from the Directorate General of Commercial Intelligence and Statistics is subject to changes and, at times, the conclusions drawn could be different.
- **Time lag issues**- e.g. Both CMIE and NSSO are compiled over months, and this means they do not capture data at a particular point of time.
- **Politicisation of Data**-which has led to inflation and deflation of statistics to suit one's own performance, which does not corroborate with other crucial statistics. E.g. Divergence between high growth and low jobs in India.
- **Erosion of autonomy of institutions**- Senior officials of National Statistics Commission resigned recently over the holding back of jobs data.

Success Story of Indian Statistics- The RBI

- The **monetary and banking data** of the Reserve Bank of India is probably the best in the country and respected everywhere.
- This is possible because the data flows from a regulated set of entities, which have to comply with the structures.
- The presentation of accounts by banks has been homogenised to ensure that there is no ambiguity in definitions, and hence there are no revisions in the data.

Restructuring of Statistical System

Recently, the government has decided to merge the Central Statistical Organisation (**CSO**) and the National Sample Survey Office (**NSSO**) to form a National Statistical Office (**NSO**), under the **Ministry of Statistics and Program Implementation** (MoSPI).

Benefits

- This move will streamline the administrative functions with the involvement of Directorate General level officers in administrative and overall coordination of the ministry.
- The Data Processing Division (DPD) of the present NSSO would be renamed **Data Quality Assurance Division (DQAD)** and have the responsibility to bring out quality improvements in survey data, as well in data of non-survey source like Economic Census and administrative statistics (provided by various department or bodies).
- However there are questions over the **loss of autonomy of NSSO.** Earlier, NSSO was an attached office of MoSPI, which gave it a legally distinct identity from the ministry. National Statistics Commission used to oversee all technical aspects of the statistical work—which survey needs to be done, when and how it needs to be done. With the merger of NSSO and CSO, the autonomy of NSSO will go away and the NSC's control over NSSO will not be there.
- Statistics should have an independent oversight and inputs. Recently, the **Indian Council of Social Science Research** has initiated a new programme called the **Impactful Policy Research in Social Sciences**. Such, independent research requires timely access to reliable and neutral macro statistical data.
- As recommended by the **Rangarajan Committee**, the NSO should work as the nodal body for all core statistical activities, but it should work under a separate body, which is directly answerable to the Parliament, not the government. The body must be mandated the role by giving a statutory status. Without such a move, the Parliament may not be able to uphold the accountability of the government.

Implications

- **Widening Trust Deficit on country's official data**- particularly on the GDP growth and employment/unemployment.
- **Investors and Industries**- get impacted due to lack of predictability towards the country's economy.
- **Ineffective Policy Response**- e.g. Reserve Bank of India's monetary policy decisions often go astray because of erroneous data provided by the government, as remarked by a former RBI Governor. This also **impacts developmental efforts** of the government.
- **Absence of public accountability**- as there is lack of access to data for interested stakeholders. It also impedes policy implementation.

* **Impact on Public Discourse**- statistical integrity is crucial for generating data that would feed into economic policy-making and that would make for honest and democratic public discourse.

Way Forward

* The government should swiftly work on finalizing the draft **National Policy on Official Statistics**.
* Whenever the base for national accounts is updated—as it should be to incorporate **conceptual changes, statistical changes** (such as methodological upgrades) or results of new surveys conducted closer to the base year—the old series should be routinely linked to the new series for providing comparable data.
* The NSC should be reconstituted at the earliest and steps taken to empower it with adequate resources as an independent watchdog. NSC should be the sole agency responsible for official statistics and reporting only to the parliament. In the long term NSC should be a statutory body.

Draft National Policy on Official Statistics

* **Core statistics:** The draft policy proposes to focus on certain statistics of national importance as core statistics
* **National Statistical Commission** (NSC) be re-constituted to regulate and audit core statistics and advise the central government on improving other official statistics
* A **National Statistical Appraisal and Assessment Organisation** will be set up under NSC to conduct statistical audits.
* A **National Statistical Development Council** will be set up under the chairmanship of the Prime Minister to provide guidance to the NSC on policy matters
* **All-India Indian Statistical Service**: Currently, there are several statistical cadres such as the Indian Statistical Service, State Statistical Services, and other Group A Statistical posts or cadres.

* **Rather than strive for speed** in disseminating data on a more real-time basis, it would be better to tarry and **provide final numbers** even if there are lags involved. This would avoid the embarrassment of changing the discourse or commentary when reacting to new numbers.
* India's fiscal data system should be developed in the framework of **'information' federalism** wherein cooperation, coordination and competition among the different tiers of federal governance would build up a modern state-of-the-art fiscal data system.

3.1.3. GDP ESTIMATION IN INDIA

Why in news?

* Recently, there has been a controversy over India's new GDP series and its estimation methodology.
* In a recent published research paper, Former Chief Economic Adviser Arvind Subramanian had concluded that the country's growth has been overestimated by around 2.5% between 2011-12 and 2016-17.

Changes made in Indian GDP Series

In 2015, the Central Statistics Office came up with a revised methodology **for the calculation** of GDP of the country.

* **Change of base year to 2011-12 (from 2004-05)** to capture the unorganized sector data from NSSO's Employment-Unemployment Survey (EUS) of 2011-12.
* **Incorporation of Recommendations of System of National Accounts (SNA), 2008:**
  * Valuation of **Gross Value Added (GVA)** & Net Value Added (NVA) at **basic prices**
  * Considering **GDP at market prices as headline GDP** instead of GDP at factor cost, to make the new calculation more **consumer-centric.**
  * Treating **unincorporated enterprises** maintaining accounts as quasi-corporations
* **Incorporation of MCA21 database:** Ensuring comprehensive coverage of corporate sector in mining, manufacturing & services.

Gross Domestic Product (GDP) vs Gross Value Added (GVA)

* Gross Domestic Product (GDP) is the **monetary value all final economic goods and services** produced in a country during a specific period of time.
  * Domestic territory means **political frontiers of the country** including its territorial waters, commercial vessels operated by country's residents etc. & also **includes country's embassies & consulates located abroad.**
* GVA is **measure of value added** in goods and services produced in economy **i.e. GVA = economic output – input.**
* **GVA is sector specific while GDP is calculated by summation of GVA of all sectors** of economy with taxes added and subsidies are deducted.
* **Central Statistics Office (CSO)** in the **Ministry of Statistics and Programme Implementation (MoSPI)** is responsible for the compilation of National Account Statistics including GDP.

- Earlier, contribution of enterprises was assessed using **Index of Industrial Production** & **Annual Survey of Industries**.
- **Broader coverage of financial sector** by including stock brokers, stock exchanges, asset management companies, mutual funds and pension funds, as well as regulatory bodies, SEBI, PFRDA and IRDA.
  - Earlier estimates primarily covered commercial banks and NBFCs.
- **Adopted Effective Labour Input (ELI) Method:** Earlier, it was assumed that all categories of workers contribute equally. New method **addresses differential labour productivity issue** by assigning weights to different categories of workers based on their productivity.
- **Use of results of recent surveys and censuses:** Current data from latest surveys have been incorporated in the GDP calculation. E.g. Agricultural Census 2010-11; All India Livestock Census, 2012; All India Debt and Investment Survey, 2013 etc.

Benefits of adopting new series

- India has been able to **numerically improve its GDP estimates**.
- It would improve **India's sovereign credit rating** and **bring in more foreign investment**.
- It would also help India to claim bigger **quota at IMF**
  - Quota determines country's subscription to IMF, access to fund & voting rights to influence lending decisions.
  - Current quota formula is weighted average of GDP (50%), Openness (30%), Economic Variability (15%) and International Reserves (5%).

MCA-21 Database

- It is an e-governance initiative that was launched in 2006 to allow firms to **electronically file their financial results and advance filing of corporate accounts,** to calculate national accounts.
- It allows for a **more granular approach**, looking at the balance sheet data of each company and aggregating the performance of the sector from that, after adjusting for inflation.
- It also include addition to the **volume index of Index of Industrial Production (IIP) and establishment-based dataset of Annual Survey of Industries (ASI).**

Issues in GDP Estimation in India

Concerns about the **accuracy of India's new GDP series** stems from legacy problems with the national accounts system in the country, which were either left unaddressed or were aggravated during the base year change exercise in 2014-15.

- **Volatile Revisions:** The revisions (between advance estimates & revised estimates) in overall GDP numbers tend to have an upward bias, which raises questions on the credibility of GDP data. Moreover, volatile revisions create challenges for policymakers who make decisions based on initial estimates.
- **Overestimation bias in informal sector:** The new GDP series assumes that the informal manufacturing ('quasi-corporations') sector grew at the same rate as the formal manufacturing sector, which might have inflated informal sector growth in the new series.

GDP Deflator

- **GDP price deflator** is a ratio of price levels in two different years that accounts for inflation in the prices of goods and services.
- *GDP Deflator = Nominal GDP at Current Prices (2018) / Real GDP at Constant Prices (Base Year 2011) ×100*
- Quantitatively, the production may not have improved and the growth rate may appear to be high only because of inflation in the prices.
- GDP Deflator enables comparisons of real GDP from one year to another.

- **Use of Deflators:**
  - Wholesale price index (WPI) as deflator for several sectors of the economy (particularly services) is inappropriate.
  - Currently, in GVA calculation, instead of deflating output and input with their respective prices, common output deflator is used, which assumes that input & output prices move in same direction and thus, creates a bias. E.g. when oil prices were low, and input inflation was falling, while output inflation continued to rise, there had been a tendency of growth overestimation.
- **Use of MCA21 database:** The use of an untested corporate database, MCA-21 and the manner in which it is used in National Accounts for calculation under new GDP series is contentious.
  - MCA-21 database also **lacks state-wise details**, which has **distorted state-level GDP**. These changes have enormous implications for the **borrowing limits of states** (3% of GSDP as mandated by FRBM Act 2003), and on the **devolution of resources to states by the Finance Commission.**
    - ✓ Most of the relatively prosperous states such as Delhi, Kerala and Karnataka saw a further boost to their GSDP, which allowed them to borrow more.
    - ✓ Some states like Bihar and West Bengal saw their economies shrink, forcing them to reduce spending to meet fiscal deficit targets.

✓ Devolution of funds by Finance Commission will be impacted as formula includes both fiscal performance & income distance.

Income distance measures the difference between the per capita GSDP of a state and the per capita GSDP of the state with the highest per capita income.

- **Shift from establishment to enterprise approach:** The new GVA methodology shifted data collection from establishments (or factories) to enterprises (or firms). All the value added at enterprises classified as "manufacturing firms" goes into the calculation of manufacturing GVA. But, the activities of firms are much more diverse than factories (e.g. some subsidiaries may only look into services like transportation) and would not qualify as manufacturing.
- **Administrative Issues:** Lack of transparency and effective audit of the GDP database point to **inadequate oversight** of the Central Statistics Office (CSO), which is responsible for the National Accounts Statistics.

Way Forward

- **Existing data sources** including MCA21 database should be properly **authenticated** before plugging it into National Account Statistics.
- **New data sources and methodologies** can be explored e.g. using transactions-level GST data to estimate expenditure-based estimates of GDP.
- The shift from **establishment approach** to **enterprise approach** will be successful only if all the disaggregated information in MCA21 database on activities of a firm is classified properly into appropriate sectors.
- Greater **transparency** on the methodology and **better data dissemination standards** can help improve the credibility of the official GDP numbers. The recent **merger of Central Statistics Office (CSO) and National Sample Survey Office (NSSO)** can help CSO to adopt transparent data practices of the latter.
- Growth rates are critical for internal policy making as it has a bearing on both monetary and fiscal policies. E.g. If we over-estimate the growth rates, we might keep interest rates too high from a cyclical perspective, which might prolong growth stagnation. Therefore, it is important to see the broader message behind the concerns raised and make the process of GDP estimation more robust according.

3.1.4. MIDDLE INCOME TRAP

Why in news?

Recently, a member of PM Economic Advisory Council (PMEAC) warned that India may be nearing a structural slowdown and may soon get caught in the 'middle income trap' like Brazil and South Africa.

What is middle-income trap?

- The term middle-income trap (MIT) usually **refers to countries that have experienced rapid growth and thus quickly reached middle-income status** (with Gross National Product per capita between $1,000 & $12,000), **but then failed to overcome that income range** to further catch up to the developed countries and achieve high-income status. MIT is a relatively new phenomenon and was first mentioned in 2007 in the World Bank report.
- The countries caught in the MIT are unable to compete with low-income, low-wage economies in manufactured exports and unable to compete with advanced economies in high-skill innovations.
- MIT is **associated with a relatively sustained growth slowdown** with both direct effects (e.g. income losses) as well as indirect effects (e.g. social conflicts).
- Fuelled by the global slowdown, many countries, particularly in South East Asia (e.g. Thailand, Vietnam, and Malaysia etc.), Africa (e.g. South Africa) and Latin America (e.g. Brazil) currently face the predicament of MIT, which has impeded their transition from middle income to high income.

Why Do Countries Fall into the Middle Income Trap?

- **Inability to shift growth strategies**: If a country cannot make a timely transition from resource-driven growth, with low-cost labor and capital, to productivity-driven growth, it might find itself trapped in the middle-income zone.
    - Traditional exports cannot be as easily expanded as before because wages are higher and cost competitiveness declines.
    - Moreover, export growth depends on introducing new processes and finding new markets. To do this, exporters must understand the quality, price, and consumer preference points of the global economy, which is a demanding task.

- **Skewed income distribution & stagnation in middle class population**: Wealth inequality and the hierarchical distribution of income in developing countries is a downward drag on domestic demand, which results in stagnation. It slows down the upward mobility of families that are at lower levels, into middle class that is prepared to pay more for quality and differentiated products.
- **Recurring boom-bust cycles & procyclical lending**: Many middle-income countries in Latin America have been through cycles of growth based on credit extended during commodity booms, followed by crisis, and then recovery. This stop–go cycle has prevented them from becoming advanced economies despite enjoying many periods of fast growth. This is in sharp contrast with successful countries in East Asia—Japan, Hong Kong, Taiwan, Singapore, and South Korea that have been able to sustain high growth over some 50 years.

Why India might get caught into middle-income trap?

- **Backlash against globalization**: Hyperglobalization (that benefited the early convergers like China, South Korea & Japan) led to a backlash in the advanced countries, as seen through increasing protectionism & lowering World Trade-GDP ratios since 2011. This means that similar trading opportunities may no longer be available for the new convergers.
- **Thwarted Structural Transformation**: Successful development requires two kinds of structural transformations: 1) a shift of resources from low productivity to high productivity sectors; and 2) a larger share of resources devoted to sectors that have the potential for rapid productivity growth. However, in late convergers like India, 'pre-mature deindustrialization' (tendency for manufacturing to peak at lower levels of activity and earlier in the development process) is a major cause of concern.
- **Human Capital Regression**: Human capital frontier for the new structural transformation has shifted further away making the transformation costlier. This is because the new advents in technology not only require skilled human capital, but also demands them to learn continually. As opposed to these requirements, there is a wider educational attainment gap between lower income countries and advanced economies.
- **Climate change-induced Agricultural Stress**: Agricultural productivity is crucial both for feeding people and for ensuring human capital moves from agriculture to modern sectors. With climate change, ambient temperature has increased and weather extremities have become a recurrent phenomenon. This is, in particular, a threat to India where agriculture is heavily dependent on precipitation.
- **Fall in private consumption, muted rise in fixed investment and sluggish exports** have led to slowdown in the economy and increase India's vulnerability to the middle-income trap.

Avoiding the Middle Income Trap

- **Transitioning from diversification to specialization in production:** Specialization allowed the middle-income Asian countries to reap economies of scale and offset the cost of disadvantages associated with higher wages (E.g. Electronics industry in South Korea).
  - High levels of investment in new technologies and innovation-conducive policies are 2 overarching requirements to ensure specialized production.
  - Developing good social-safety nets and skill-retraining programs can ease the restructuring process that accompanies specialization.
- **Shifting to productivity-led growth**: Total factor-productivity growth in middle-income countries requires major changes in education, from primary & secondary schooling to tertiary education so that workers are adept in new skills as per the demands of the markets. Creating such knowledge economy requires long term planning and investment.
- **Opportunities for professional talent**: To attract and retain a critical mass of professional talent that is becoming more internationally mobile, middle-income countries like India must develop safe & livable cities that provide attractive lifestyles to professionals.
- **Addressing barriers to effective competition**: There is a need to address rigidities that can arise from bankruptcy laws, stringent tax regulations, limited enforcement of IP regulations, imperfect information, discrimination etc.
- **Decentralized economic management**: Greater powers should be vested in local governments to ensure speedier decision making
- **Sustaining macroeconomic stability** through flexible fiscal framework that limited deficits and debt, and a flexible exchange rate mechanism backed up by a credible inflation-targeting monetary policy could help

sustain long periods of growth. Effective restructuring, regulating, and supervising of the financial sector must be ensured so that the present NPA crisis can be effectively handled.

- **Changing orientation of social programmes** that targets middle class besides poorer sections of the society, which would propel the demand driven growth. E.g. low-cost housing for first-time home buyers in cities, programs to ensure that recent graduates get suitable employment opportunities, paying more attention to public goods like safety, urban transport, and green spaces etc.

3.2. RESOURCE MOBILISATION

3.2.1. INDIRECT TAXATION- TWO YEARS OF GST

Why in news?

Hailed as the biggest tax reform, GST has completed 2 years of operation. It was launched on 1st July, 2017 in a special session of Parliament.

About Goods and Services Tax (GST) and its present structure

- GST is a **destination-based indirect tax** and is **levied at the final consumption point**.
- Under GST, a gamut of **17 indirect taxes** like excise duty, VAT, service tax, luxury tax etc are subsumed.
  - **Taxes not subsumed under GST:** Basic Custom Duty, Anti-Dumping Duty, Central Excise on Petroleum Products, VAT on alcohol for human consumption, Stamp Duty, Property Tax (levied by local bodies), Professional Tax etc.
- GST is currently levied on every product [except **petroleum products, alcohol, real estate & electricity**] in four slabs of **5, 12, 18 and 28%.**
  - Most of the daily use articles have zero GST as per the latest revision of the tax rates last year.
  - In addition, a cess is levied on automobiles, luxury, and demerit and sin goods.

Key terms associated with GST

GST council

- It is a **constitutional body** under article **279(A)** for making recommendations to the Union and State Government on issues related to GST.
- It is chaired by the **Union Finance Minister** and **other members** are the Union State Minister of Finance and Ministers in-charge of Finance of all the States.

GSTN

- Goods and Services Tax Network (GSTN) is a **not for profit company** governed under section 8 of the **companies Act.**
- The Company has been set up primarily to provide **IT infrastructure and services** to the Central and State Governments, tax payers and other stakeholders for implementation of the Goods and Services Tax (GST).

Reverse Charge Mechanism

- The GST has to be typically paid by the supplier of goods and services. But in some cases, the liability to pay the tax falls on the buyer. This is called reverse charge.
- This is only applicable in certain instances e.g. when a business buys goods or services from a supplier who is not registered to pay GST or in cases of import.

GST Composition Scheme

- Taxpayers registered under this scheme pay a small tax (1%, 5% or 6%) on their turnover.
- It reduces administrative burden of taxpayers but makes it difficult for them to sell to larger firms as they are not eligible for input tax credits.

E-way Bill (Electronic-way bill)

- It is a document introduced under the GST regime that needs to be generated before transporting or shipping goods within state or inter-state.

- From Government's perspective, it is **easier to collect** and **reduces tax evasion**, for customer it is **easier to understand** & will **reduce tax burden** and for industry, it ensures that there is **no cascading effect of the tax** and there is **harmonization of tax laws, procedures and rates of tax**

Successes of GST

GST marks a fundamental **resetting of the Indian economy**. It redefines the way business is done (with increased formalisation), expands the market for goods and services (replacing many small and fractured markets with a single common one) and totally overhauls the Indirect Tax regime (one nation one tax regime)

- **Tax Compliance:**
  - GST has been **successful in increasing compliance** among small traders through **Composition Scheme**. At present, small dealers up to a turnover of Rs 1.5 cr can opt for composition scheme and pay only 1% tax, **facing a lesser compliance burden**.
  - There is now a single online system from filings to returns that has made transactions more transparent.

- Self-policing mechanism of GST helps to check tax evasion and expand the tax net
  - ✓ Seamless flow of input tax credit is possible only when all the suppliers of a business pay GST. So each business will make sure that its suppliers have paid the GST, so that they can take input tax credit.
  - ✓ By putting the burden of paying the tax on the buyer (**called reverse charge**), in cases where the supplier does not pay GST, the Government is nudging all businesses to sign up for GST.

Recent Changes in GST Regime

- **Changes to GSTN:** Currently the centre holds 24.5% equity and the States (including UTs Delhi and Puducherry) hold 24.5% equity in GSTN. The Balance 51% equity is with non-Government financial institutions.
  - The restructured GSTN will have 100% government ownership equally distributed between the Centre (50%) and the States (50%).
- **Setting up of Goods and Services Tax Appellate Tribunal**: It is a quasi-judicial body that will mediate in indirect tax disputes between states and centre.
- **Relief to MSME sector**
  - **Higher Exemption Threshold Limit**
  - **Increase in Turnover Limit for the existing Composition Scheme**
  - **Composition Scheme for small services provider**
- **Measures to boost exports**- Relief has been given to exporters by giving them an option to export without payment of tax, by submitting a simple letter of undertaking on their letter heads.
- **Changes in GST Rates:** GST council decided to cut tax rates on 23 goods and services. Now, the 28 per cent slab is restricted to only luxury and sin goods.

- **Revenue Base:** GST has helped the Government to **expand the revenue base** by about 85% in the past two years from 65 lakhs to 1.2 crore.
- **Revenue Collections and Buoyancy:** The relative buoyancy of GST revenue compared to the pre-GST period is a result of two factors. 1) the design of GST that integrated the entire value chain from raw material to retail for the purpose of indirect taxation. 2) The tax incidence on services increasing from 14% pre-GST to 18% post-GST.
- **Rationalization of taxes:**
  - Currently, **around 97.5% articles are covered by 18% or lower GST slab**, a significant reduction from tax rates under the VAT regime where standard VAT rate was 14.5% and excise duty was 12.5%.
  - **A good fiscal system should not tax the production of intermediate goods**. It is a destination tax that is collected at the point of final consumption.
- **Re-engineering of supply chain:** GST has presented an opportunity to reduce physical supply chain costs (costs attributable to transportation, warehousing, inventory, etc.)
  - A unified tax and seamless availability of credit has reduced the cost of procurement of raw material**.**
- **Introduction of E-Way Bills:** Introduction of E-Way bill marks a shift from departmental policing model to self-declaration model for movement of goods
  - It would enable hassle free movement of goods by **eliminating the requirement of separate transit pass** for each state.
  - Government has introduced several changes in e-way bill system including **auto-calculation of distance based on PIN codes** and **blocking generation of multiple bills on one invoice** to make the system more efficient
- **Use of technology:** All the operations ranging from front-end services of registration, returns and payments to all taxpayers, as well as the backend IT modules for States that include processing of returns, audits, assessments, appeals etc. have been digitalized
  - **Reduced the interface** between tax collector and taxpayer, thereby reducing the scope for corruption.
  - **High quality quantifiable data** on the formal-informal, state specific production, state-wise distribution of exports, point of origin of goods/services, and other economic data will enable better policy making and governance.
  - Per capita gross state domestic product has a high correlation with exports. Use of GST data can significantly **improve GDP estimation**.
- **Reinforces Cooperative Federalism: GST council** has emerged as a successful example of cooperative federalism and its functioning has been free from political biases**.**

Challenges that still remain

- **List of exclusions:** Petroleum products (crude oil & natural gas), diesel, petrol, aviation turbine fuel, potable alcohol and real estate, which contribute 35-40% of indirect tax revenue, are still out of GST's ambit.

- **Complex GST Structure with multiple tax slabs:**
  - **4 different rates** undermine eventual goal of simplifying tax compliance & leads to foregoing of efficiency gains. It is incongruent with globally acceptable practice of single GST.
  - **Administering multiple rates** is challenging, such as high cost of auditing the classification of products into exempt, high & low tax slabs across every stage of production, distribution & consumption and long-standing litigation in case of disputes.
- **Digital infrastructure and data privacy:**
  - Implementation of GST required **registration at humungous scale** for input based tax crediting and **creating a common database of registered traders to be managed centrally**. This has emerged as a major challenge to GST's IT landscape. Until now, states maintained the database individually.
  - **Technical glitches** e.g. Introduction of E-Way Bill was delayed due frequent website crashes
- **Anti-profiteering norms:**
  - Provisions in Central GST legislation require industry to reduce prices and pass on the net benefits arising from implementation of the GST to end consumers to keep inflation under control. But, implementation of the regulations is facing several roadblocks.
  - Power given to taxmen to conduct 'mock purchases', visit premises, search and check invoices might lead to misuse.

Way Forward

- **GST taxable base must include petroleum products**, especially aviation turbine fuel and natural gas, real estate and electricity. Inclusion of real estate will clean up the land market and will lead to revenue gains on direct tax side as well as more transactions will be reported.
- Although indirect taxes tend to be regressive in nature, a **low standard or modal rate with a small list of exemptions** is the ideal GST structure that Government should try to achieve.
  - **World Bank study** said that the Indian GST rate was 2nd highest among the 115 countries with a national value-added tax. It was also the most complicated, with five main tax rates, several exemptions, a cess and a special rate for gold.
- **Revenue performance of Composition Scheme** needs to be improved by ensuring better compliance among small traders. **Imposition of additional duty on Reverse Charge Mechanism** to be paid by Composition Dealers could be an important anti-evasion measure.
- A **single authority for sanctioning and processing GST refunds** has been proposed to simplify the procedure for exporters. Under the proposed reform, a single tax office will assess, check and sanction refunds of both centre and state GST portions

Conclusion

- Governments pushing reforms have to beat the political costs upfront and early, with the benefits evolving over the medium term.
- Although it is at its early days still, the GST started on a positive note and the benefits for all stakeholders are evident. It is now time for the Government to stabilise the system, remove uncertainty, facilitate compliance by easing processes and expand the tax base to make the GST a real success.

3.2.2. DIRECT TAXATION

Why in news?

Recently, government stated that, there has been significant improvement in direct tax collection in the last few years.

Trends of Direct Tax collection

- There has been a growth of more than 80% in the number of returns filed in the last four financial years and direct tax-GDP ratio rose to 5.98% in FY 2017-18, the highest it has been in the last 10 years.
- Further, the number of persons filing income tax returns also increased by about 65% during period from 2014-2018.
- Moreover, **Direct Tax-GDP ratio rose** to 5.98% in FY 2017-18, which is highest in the last 10 years. This shows a sign of improvement of **Tax-Buoyancy** in the economy.

Related Information

- **What is a Direct Tax?**
  - These are the taxes, paid **directly to the government by the taxpayer.** Under the direct tax system, the incidence and impact of taxation fall on the same entity, which cannot be transferred to another person.
  - It is termed as **a progressive tax** because the proportion of tax liability rises as an individual or entity's income increases.
  - **Examples**- Income tax, corporate Tax, Dividend Distribution Tax, Capital Gain Tax, Security Transaction Tax.
- The system of Direct taxation is governed by the **Central Board of Direct Taxes (CBDT).** It is a part of the Department of Revenue in the Ministry of Finance.

Tax Buoyancy

- It is calculated as a ratio of percentage growth in tax revenues to growth in nominal GDP for a given year.
- It is an important indicator of the efficiency and responsiveness of tax revenue mobilisation to GDP growth.

Crowding Out Effect

- It describes the idea that large volumes of government borrowing push up the real interest rate, making it difficult or close to impossible for individuals and small companies to obtain loans.

Reasons for increase in Direct Tax collection

- **Growing Economy:** Countries' national income level has been improving over the next few years and its transition into middle-income economy has led to increase in tax base.
- **Goods and Service Tax:** Under the GST provisions business entities have to disclose their annual turnover, this makes direct tax evasion a difficult task.
- **Use of Digital platform:** The increase in the use of information being collected digitally by the tax department increased the efficiency in tax collection and helps in checking of tax evasion.
- **Hassle Free Refund**: Small and medium taxpayers are getting easy tax refunds. This has boosted the taxpayer confidence in taxation system of the country, thus resulting into higher tax collection.
- **Demonetisation:** Demonetisation has removed the anonymity attached to cash deposit in banks. Thus, giving rise to an inquiry, whether the amount deposited is in consonance with the depositor's income.
- **Government Initiatives** had also contributed to sound rate of Direct Tax collection, these initiatives include;
  - **Income Declaration Scheme:** It offers an opportunity to tax defaulters to disclose their income under the Income Tax Act.
  - **Aaykar Setu:** It is an app to help users, to understand the various nuances of direct taxes, file income tax, apply for PAN, check TDS statement etc.
  - **Project Insight:** It will monitor high-value transactions with **use big data analytics to** find out any discrepancy between a taxpayer's income and expenses.
  - Increased surveillance from **linking Aadhar to Permanent Account Number (PAN)** and to bank accounts.
  - A task force has been constituted under **Arbind Modi** for drafting a new direct tax legislation.

Significance of Direct tax collection

- **High Tax buoyancy:** It is an important metric to know the expected level of government borrowings from the debt market. Higher tax buoyancy would mean the **government would borrow less** — keeping interest rates lower — **while giving room for corporates also to borrow at lower rates** thus reducing **crowding out effect** in the economy.
- **Fiscal Health:** High rate of direct tax collection increases spending capacity of government on social sectors such as education and health, without compromising the **fiscal prudence** in the economy.
- **Maintaining Inflationary Trends:** High rate of direct tax collection helps in maintaining the optimum interest rate in the economy, which in turn assists in maintaining the inflationary pressure.
- **Lower Indirect tax:** Higher direct tax collections could lower the tax burden on the poor by creating fiscal space for a reduction in GST rates.

3.2.3. NATIONAL INVESTMENT AND INFRASTRUCTURE FUND

Why in news?

Off late, the National Investment and Infrastructure Fund (NIIF) has been adopting various approaches to mobilize resources for funding infrastructure projects.

About NIIF

- NIIF is India's **first sovereign wealth fund** that seeks to create l**ong-term value for domestic and international investors** seeking investment in **Greenfield, Brownfield and Stalled** infrastructure projects.
- This fund will invest only in **commercially viable projects**, which can pay back returns.
- NIIF is registered with SEBI as a **Category II Alternative Investment Fund** with a planned corpus of Rs. 40,000 crore.
- It is a **quasi-sovereign wealth fund**, where **49 percent** stake is with the Government and the rest held by marquee foreign and domestic investors such as Abu Dhabi Investment Authority, Temasek and HDFC Group.
- It is run as a professional body with a full time CEO. But, Governing Council headed by **Finance Minister** oversees the activities.

Alternative Investment Fund

- It refers to any privately pooled investment fund in form of a trust or a company or a body corporate or limited liability partnership, which do not come jurisdiction of any regulatory agency in India.
- AIFs have been defined in Regulation 2(1)(b) of SEBI (Alternate Investment Fund) Regulations 2012. And its definition includes venture capital fund, hedge fund, private equity fund etc.

Sovereign wealth fund

- It consists of pools of money derived from a country's reserves, set aside for investment purposes to benefit the country's economy and citizens.
- The funding for a sovereign wealth fund comes from central bank reserves that accumulate as a result of budget and trade surpluses, and from revenue generated from the exports of natural resources.

Different Approaches adopted by NIIF

- **Investment through different types of funds-**
    - **Master Fund-** for primarily investing in operating assets in core infrastructure sectors such as roads, ports, airports, power etc.
    - **Fund of Funds-** for investing with experienced fund managers who have a strong track record and enable them to attract further institutional investors to invest in their funds.
    - **Strategic Fund-** aimed at growth and development stage investments in projects/companies in a broad range of sectors that are of economic and commercial importance and are likely to benefit from India's growth trajectory over the medium to long-term
- **Monetization of assets-** by converting non-revenue generating assets into sources of revenue.
- **Tapping Sovereign Funds-** by channelizing money of other countries into India. E.g.-
    - Partnering with Abu Dhabi Investment Authority (ADIA) focused on ports, terminals, transportation and logistics businesses in India.
    - India and the UK announced joint UK-India Fund, namely a Green Growth Equity Fund that aims to leverage private sector investment to invest in green infrastructure projects in India.
- **Directly Investing in Infrastructure-** by using the revenue generating through its various sources. Some examples are-
    - Partnered with HDFC in an investment platform for mid-income and affordable housing in India.
    - Acquired IDFC Infrastructure Finance Limited from IDFC.

Significance of NIIF

- Given its implementation is being done by experts, the working and management of its resources is being done with professionalism and strategic long-term vision.
- It will help move forward various stalled projects as well as greenfield projects. This in turn, helps companies to reduce their outstanding loans, thus help reducing bank bad loans. It helps in overall stimulation of the economy.
- It has adopted a different approach to go about its business and is advancing more aggressively than many such institutions created earlier like IFCI (1948), IDFC (1997) and even the currently troubled IL&FS set up in 1987.

3.2.4. STEPS TAKEN TO CURB TAX EVASION

3.2.4.1. CAPITAL GAINS TAX

Why in News?

Capital gains on investments made in India through companies in Mauritius and Singapore became fully taxable from April 1 after the concession period of 2 years ceased to exist.

More on News

- India amended the **double tax avoidance agreements (DTAA)** with the two countries in 2016, to prevent aggressive corporate tax avoidance.
- The loophole in these tax treaties had led to a situation where gains from investments into India from the two countries were taxed neither in India nor in the country where the investing entity was located.
- Now, entity from Mauritius and Singapore will have to pay capital gains tax here while selling shares in a company in India.

What is DTAA?

- The DTAA treaty is signed in order to avoid double taxation on the same declared asset in two different countries.
- These DTAAs are made to make a country attractive for investment purpose by providing relief on dual taxation. The relief is provided by exempting income earned overseas from tax in the resident country or by providing credit to the extent wherein taxes have already been paid abroad.
- India has **Double Taxation Avoidance Agreement (DTAA)** with **88 countries**, but presently **85** have been in force.

Capital Gains Tax

- Any Income derived from a Capital asset movable or immovable is taxable under the head Capital Gains under **Income Tax Act 1961**.
- Any profit or gain that arises from the sale of a 'capital asset' is a capital gain. This gain or profit is considered as income and hence charged to tax in the year in which the transfer of the capital asset takes place. This is called **capital gains tax**, which can be short-term or long-term.
- Capital gains are not applicable when an asset is inherited because there is no sale, only a transfer. However, if the asset is sold by the person who inherits it, capital gains tax will be applicable.
- **Short-term capital asset:** An asset which is held for a period of 36 months or less. Assets like equity or preference shares in a company listed on a recognised stock exchange in India, securities (debentures, bonds, government securities), equity oriented mutual funds, zero coupon bonds are considered short term if held for less than 12 months.
- **Long-term capital asset:** An asset that is held for more than 36 months (24 months for immovable property like land, building). The Long-term capital gain is taxable at 20%.

3.2.4.2. BASE EROSION AND PROFIT SHIFTING

Why in News?

The Union cabinet approved **ratification of a multilateral convention to implement OECD's project** on checking tax evasion.

About the Convention

- **The Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (BEPS)** was signed in Paris in 2017.
- It entered into force on 1st July 2018.
- The Multilateral Convention is an **outcome of the OECD/G20 Project** to tackle Base Erosion and Profit Shifting (BEPS).
- The Convention will **modify India's treaties in order to curb revenue loss through treaty abuse and base erosion and profit-shifting strategies** by ensuring that profits are taxed where substantive economic activities generating the profits are carried out and where value is created.
- The Convention enables all signatories to meet treaty-related minimum standards to counter treaty abuse and eliminate double taxation that were agreed as part of the BEPS package.

Base Erosion and Profit Shifting (BEPS)

- It refers **to tax avoidance strategies** that exploit gaps and mismatches in tax rules to artificially shift profits to low or no tax locations resulting in little or no overall corporate tax being paid.
- The OECD, under the authority of the Group of 20 countries, has considered ways to revise tax treaties, tighten rules, and to share more government tax information under the **BEPS project**, and had issued **action plans in 2015**.
- The BEPS project would:
    - **increase tax revenues** which were earlier lost due to BEPS. BEPS is of major significance for developing countries due to their heavy reliance on corporate income tax, particularly from multinational enterprises.
    - give **level playing field** for both and domestic and global companies by allowing them to conduct businesses under similar circumstances. Tax savings from BEPS give multinational companies an edge over domestic companies, who may lack the wherewithal to employ such strategies.
    - **prevent double taxation.**

3.3. DEBT AND ITS RESOLUTION

3.3.1. STATUS PAPER ON GOVERNMENT DEBT

Why in news?

According to the Status Paper on Government Debt for 2017-18, the Centre's total debt as a percentage of GDP **reduced to 46.5% in 2017-18** from 47.5% as of March 31, 2014.

Why government debt needs to be controlled?

- **Affects investor confidence:** In the absence of fiscal consolidation, there is an increased risk of default & hence, downgrading of sovereign credit ratings by the credit rating agencies. Loss of investor confidence will not only reduce FDI/FII in India but will also make future borrowing expensive.
- **Affects credit growth:** As more money is lent to government rather than invested in the market, corporate sector is crowded out leading to slower industrial and capital asset growth and potential loss of employment.
- **Fiscal repression of commercial banks:** When the government borrows more, it forces Public Sector Banks to purchase more of Government Securities (GSecs). When a commercial bank invests more in GSecs (where it earns lesser interest than commercial loans), it reduces the capital availability to private sector and affects profitability of the banks.

Government Debt

- **Government liabilities** have been broadly classified as debt contracted against the Consolidated Fund of India (defined as **Public Debt**) and liabilities in the Public Account, called **Other Liabilities**. Public Debt is **41%** of GDP, while other liabilities are **5.5%** of GDP.
- Public debt is further classified into **internal** (38.2% of GDP) and **external** debt (2.9% of GDP).
- **Internal debt** consists of **marketable** debt (32.9% of GDP) and **nonmarketable** debt (5.3% of GDP).
  - Government dated securities and Treasury Bills, issued through auctions, together comprises marketable debt.
  - Intermediate Treasury Bills (14 days ITB) issued to State Governments and select Central Banks, special securities issued to National Small Savings Fund (NSSF), securities issued to international financial institutions, etc., are part of non-marketable internal debt.
- **Other Liabilities** include liabilities on account of Provident Funds, Reserve Funds and Deposits, Other Accounts, etc.

- **Inflation:** Too much of government debt can lead to inflation and reduction in real interest rates. It might prompt people to invest more in gold and real estate, thereby accentuating the problem of poor economic liquidity and black money.
- **Exchange rate risk:** The reduced demand of domestic securities relative to foreign securities (due to poor credit rating) might push the exchange rate down and weaken the domestic currency with respect to dollar. It will make imports more expensive and further fuel inflation.
- **Committee Recommendations:** N.K. Singh-headed FRBM (Fiscal Responsibility and Budget Management) Review Committee had recommended ratio to be 40% for the Centre & 20% for the States, respectively, by 2023, which is consistent with international best practices.
- **Intergenerational parity:** It will be hurt as future generations will have to pay increased taxes to settle the government debt.

While Government borrowing is necessary to stimulate growth and aggregate demand by spending in welfare measures and capital asset development, high debt-to-GDP ratio isn't good for long term macroeconomic stability of the country.

Has fiscal consolidation worked for the central government?

- **Gross fiscal deficit (GFD)** as a % of GDP has declined from 5.9% in 2011-12 to 3.5% in 2017-18.
- **Borrowing more from market:** Government has reduced its dependence on RBI (borrowing from RBI is inflationary as it increases currency in circulation) to cover up temporary deficits in receipts and expenditures. This is evident from greater share of marketable debt.
- **Moving towards market interest rates:** The Government has also progressively moved towards alignment of administered interest rates with the market rates to remove disparity between public and private sector in market borrowing and prevent crowding out of private sector.
- **Lowering interest rate volatility:** ~98% of the public debt in India is contracted at fixed interest rates insulating debt portfolio from interest rate volatility and providing certainty and stability to budget in terms of interest payments.

- **Increasing debt sustainability:** IP-RR ratio (interest payments to revenue receipts) of Centre has decreased to 35.3% in 2017-18 from about 52% in 2000s. In India, long-term sustainability of debt is because of being largely funded through domestic savings, using largely fixed interest rate instruments, and being supported by a large domestic institutional investor base.

Strategy of central government for debt sustainability

The main objective of the Government debt management policy is to raise funds for the Government at low cost while ensuring that debt levels remain sustainable, debt structure remains stable and broader objective of financial stability is met.

Roll-over Risk
- It is a risk associated with the refinancing of debt.
- Rollover risk is commonly faced by countries and companies when a loan or other debt obligation (like a bond) is about to mature and needs to be converted, or rolled over, into new debt.
- If interest rates have risen in the meantime, they would have to refinance their debt at a higher rate and incur more interest charges in the future – or, in case of a bond issue, pay out more in interest.

- **Dedicated Body** - Institutionally, the Government has decided to setup a statutory **Public Debt Management Agency (PDMA)** to bring both, India's external (managed by Ministry of Finance) and domestic debt (managed by RBI) under one roof. The first step towards this direction was the establishment of a Public Debt Management Cell (PDMC) within Budget Division, Ministry of Finance in 2016.
- **Medium-Term Debt Management Strategy (MTDS)** - to be implemented over next 3 years (2018-19 to 2020-21) is based on three broad pillars:
    - **Low cost of borrowing**: Issuing longer tenor bonds, better investor relations and advance notifications of borrowing calendar.
    - **Risk mitigation**:
        - ✓ **Currency Risk** - Appropriate mix of domestic and foreign currency debt portfolio by improving access to foreign investors in domestic G-Sec market.
        - ✓ **Roll-over risk** - A conscious strategy of elongating maturity, from 10-year maturity bucket to 10-14 year maturity bucket, has been adopted to reduce **roll-over risk**
        - ✓ **Commodity price risks** - Launched the Sovereign Gold Bonds Scheme (SGB) to reduce demand for physical gold by providing an alternative investment instrument linked to gold prices.
        - ✓ **Interest rate risk** – Though instruments such as, floating rate bonds (FRBs), inflation indexed bonds (IIBs) and sovereign gold bonds have been issued to cater to the preferences of different investors, their contribution has remained small to limit the risk.
    - **Market development**: It would price debt efficiently.

Debt situation of states

The total debt of the States has been rising to 24% in 2017-18, and is estimated to be 24.3% in 2018-19.

Outstanding liabilities of states have increased
- **Increasing Expenditure:** due to issuance of UDAY bonds, introduction of 7th Central Pay Commission (CPC), increase in interest payments, populist measures like loan waivers etc.
- **Increasing Debts:** Post 12th Finance Commission (FC), the market borrowings of states are on the rise. Moreover, there is no institutional mechanism to incentivize higher investments in fiscally prudent states.
- **Reducing Receipts:** Centre has been levying multiple cesses, surcharges etc instead of taxes, as the proceeds need not be shared with states. It has affected the revenue collection of the states.

Steps to improve the fiscal situation
- **Improve quality of states' Public Expenditure** (ratio of capital expenditure to revenue expenditure).
    - Share of state's revenue expenditure is 80% of the total expenditure.
    - Even after the increase in quantum of "untied funds" from Centre to States (post 14th FC), expenditure of states on physical and social infrastructure has remained stagnant.
- **Re-include "Fiscal Discipline"** as a criterion in tax devolution from centre to states (not used by 14th FC)
- **More stringent, apolitical and transparent criteria** for approval of states' market borrowings under Article 293
- **Better coordination** b/w State Division Plan (approval to state borrowings) and Budget Division (monitor implementation of FRBM Act)
- Introduce **transparent accounting practices** so that there is no underestimation of State's public debt (e.g. off-budget expenses through SPSUs/guarantees issued).

3.3.2. NATIONAL FINANCIAL REPORTING AUTHORITY

Why in news?

Recently, government notified the rules determining the jurisdiction, powers, and functions of the **National Financial Reporting Authority (NFRA).**

What is NFRA?

- It is established as an independent regulator to oversee the **auditing profession and accounting standards.**
- It consists of a Chairperson, three full time members and nine part-time members.
- Chairperson and full-time members would be selected through a **search-cum-selection committee** headed by Cabinet Secretary.

Why the need arises for NFRA?

- The recent failure of **ICAI (Institute of Chartered Accountants of India)** to spot corporates fraud, raised the demand for setting up of an independent regulator NFRA.
- NFRA was one of the key changes brought by the **Companies Act 2013** but its provisions were not notified for the last five years.

ICAI (Institute of Chartered Accountants of India)

- It is a statutory body established by an Act of Parliament, viz. The Chartered Accountants Act, 1949.
- It functions under the administrative control of the **Ministry of Corporate Affairs.**
- It conducts CA exams, registers qualified CAs, issues certificates of practice etc.
- It investigates the auditors (Charted Accountants) of small listed companies **(other then entities notified under NFRA rule 2018)**
- It will provide recommendation to NFRA.

International Forum of Independent Audit Regulators (IFIAR)

- It is an **independent audit regulator from 52 jurisdictions** representing Africa, North America, South America, Asia, Oceania, and Europe.
- Its aim is to serve the public interest and to **enhance investor protection by improving audit quality globally.**
- It **shares knowledge of the evolving audit environment** and the practical experience of independent audit regulatory activity.

About the NFRA Rule 2018

- It will oversee the **auditors of banks, insurers, electricity firms** and other entities referred to it by the government.
- NFRA can investigate the auditors of:
    - Listed entities, unlisted entities with paid-up capital of not less than Rs. 500 crore or annual turnover of over Rs. 1,000 crore.
    - Those having aggregate loans, debentures or deposits of not less than ₹500 crore.
- It enables the NFRA to debar erring auditors or audit firms and it can also refer service of an auditors to **Quality Review Board** under **Chartered Accountants Act.**

Significance of NFRA

- With the constitution of NFRA, India is now eligible to become a member of the **International Forum of Independent Audit Regulators (IFIAR).**
- This shows a distinct shift from self-regulation to an independent oversight of auditors which is line with international best practices.
- NFRA will strengthen the working mechanism of ICAI because it will provide greater assurance that improper conduct will be punished which would further **strengthen the functional credibility** of ICAI.
- The rising challenges of technology require single-minded **attention to skill development**, now, ICAI will be able to pay more attention to educating and training current and future members.
- Apart from this, NFRA will have a positive impact on current **corporate governance regime** in the country.

3.3.3. INSOLVENCY AND BANKRUPTCY CODE

Why in News?

The Supreme Court recently upheld the constitutionality of the Insolvency and Bankruptcy Code (IBC).

More on the judgement

- The petitioners against IBC had argued that in the event of liquidation of the company or its sale, the **dues of operational creditors rank below those of financial creditors**, which was violative of the Article 14 of the constitution.
- However, SC said that if an intelligible differentiation can be established between two classes of creditors, **then legislation is not violative of Article 14.** The repayment of financial debts infuses capital into the economy and banks & financial institutions are able to further lend money to other entrepreneurs. Thus, relative importance of financial creditors is more vis-a-vis operational creditors.

- Further, SC said that deciding the threshold to allow withdrawal of insolvency case pertains to the domain of legislature. Moreover, the Act already contains provisions to set aside arbitrary decisions of CoC through NCLT/NCLAT.

Insolvency & Bankruptcy Code 2016: Salient Features						
Clear & Speedy Process for early Identification & Resolution of Financial Distress for corporates & Limited Liability Partnerships (LLP)	**2 distinct resolution processes:** ▪ Fresh Start ▪ Insolvency Resolution	**Adjudication Authorities:** National Company Law Tribunal (for companies and LLP) & Debt Recovery Tribunal (for individuals and unlimited partnership firms)	**Information Utilities:** To process financial information to be used in insolvency & bankruptcy proceedings	**Insolvency Professionals (IPs):** To handle commercial aspects of Insolvency Resolution Process (IRP)	**Insolvency Professional Agencies:** To develop professional standards & code of ethics for IPs	**Regulator:** Insolvency & Bankruptcy Board of India for IPs, IPAs & Information Utilities

SEQUENCE OF STEPS UNDER THE IBC

On Day 1 of the default, a creditor or a borrower can approach **NCLT/ DBT** to initiate insolvency proceedings. NCLT/DBT has to accept or reject the plea within 14 days

→ Once the case is admitted, lenders will constitute committee of creditors (CoC), appoint an **IP** which will run the borrowers' company in the interim period

→ **Within 180 days**, the CoC has to decide on a debt recast plan. Lenders will be given **additional 90 days** to arrive at a final resolution plan

→ If the lenders agree (by voting), the CoC would go ahead with debt restructuring. **Otherwise**, after 180 days, the company's/ borrower's assets will be **liquidated**

Successes of Insolvency and Bankruptcy Code

- **Promising start:** 1322 cases have been admitted by National Company Law Tribunal (NCLT). 4452 cases have been disposed at pre-admission stage.
- **Resolution at pre-admission stage:** Once a petition of the creditor is filed before the NCLT, many debtors have started paying at the pre-admission stage so that the declaration of insolvency does not take place. This indicates that IBC has pushed successful resolution outside the courts through negotiation, arbitration & reconciliation, which will lessen the burden of judiciary system.
- **Resolution of large accounts:** In June 2017, RBI had recommended 12 large accounts (having more than Rs 5000 cr of outstanding loans and accounting for 25% of total NPAs of banks) for immediate resolution under IBC.
    - Successful resolution of Bhusan Steel helped the banks successfully recover almost 75% of the total debt through 36400 cr transparent bid by Tata Steel.
- **Reduced time for resolution:** According to Insolvency and Bankruptcy Board of India (IBBI) data, the average time for resolution and liquidation outcomes is within the 270-day outer timeline. This is a significant improvement over World Bank's estimate in 2015, which stated that average time period for resolution is 4.3 years.
- **Reduced loss in recovery:** According to IBBI data, the recovery rates for financial creditors have improved on an absolute basis.
    - World Bank's Ease of Doing Business Report 2015 had observed that the debt recovery rate in India hovered around 27 cents to the dollar, and OECD countries had a recovery rate of 70 to the dollar.
- **Impact of the law on credit markets:** Operational creditors find the Code an effective tool for realising their claims. Earlier, operational creditors, comprising largely vendors and employees had no effective remedy for recovering their dues, except civil suits and the initiation of winding up proceedings before the court against the debtor.
- **Impact of Section 29(A):** After the introduction of Section 29(A), companies are paying up in anticipation of not crossing red line and being referred to NCLT. This has created a deterrent effect on potential defaulters, as they fear loss of their position in company's management if the IBC proceedings are initiated.

> **Section 29A** prohibits wilful defaulters, promoters/management of company having non-performing debt for over a year or disqualified directors from participating in the resolution process. Earlier, errant promoters could participate in the resolution process allowing them to retain control over the company and reducing their debt liability at the same time.

- **Uniform and universal application:** Generic framework of IBC has been universally adopted, as RBI has withdrawn other resolution schemes such as Strategic Debt Restructuring (SDR) Scheme, Scheme for

Sustainable Structuring of Stressed Assets (S4A) etc. This has provided consistency in the insolvency process across the country.

- **Transparency in real estate:** The amendment in 2017 allows homebuyers to be treated at par with financial creditors. It will protect the interests of homebuyers, who contribute more capital to builders than financial institutions, but so far had no say in the resolution plan.
- **Focus on Outcome Neutrality:** IBC views both revival and liquidation as means of resolving firm stress & leaves the decision to the commercial judgment of the creditors of the company. It marks fundamental shift from the thinking that prevailed in the pre-IBC world. Laws like Sick Industrial Companies Act, or Companies Act had a general aversion to liquidation as an outcome, thereby, increasing delays and pendency.

Challenges

- **Infrastructural constraints:** With the existing infrastructure & capacity of IBC, it would be difficult to deal with the volume of case flow, and the quantum of litigation being generated in the timelines that the law prescribes.
- **Substantive issues:** IBC is a nascent law with evolving jurisprudence, and the initial cases are taking more time as substantive issues are being settled by courts like validity of Section 29(A).
- **Perceived Bias against liquidation:** It is based on the belief that the objective of the IBC is to resolve stressed companies by reviving them, and liquidation represents a failure of the IBC process. The IBC amendment lowering the vote threshold (from 75% to 66%) required to approve a resolution plan also suggests this bias. In many of the ongoing cases, the process of submission of resolution plan and their evaluation is continued beyond stipulated 270 days. This is against the spirit of IBC, which puts liquidation as an outcome for stressed companies on equal footing, as revival or restructuring.
- **Challenges in liquidation process:**
  - Liquidators under IBC require lenders to relinquish control (right to sell the asset if borrower fails to repay the loan) over the company's assets, pledged as collateral for loans. Ensuring compliance in this regard has faced many legal hurdles.
  - The attachment of assets by the probe agencies like enforcement directorate (ED), income tax agency etc. for past investigations contributes to the delays. An asset entangled with Law Enforcement agencies doesn't attract many buyers.
  - Complicated land ownership patterns of the corporate debtor further poses challenges to liquidation. In many cases, liquidation cost is higher than the available assets.
- **Sanctification of the small:** Promoters of small companies are exempted from disqualification criteria under Section 29A; otherwise these companies would go directly into liquidation in absence of any bidders. However, small companies also dominate the list of insolvent companies, despite the public focus on large cases. The special status given to small companies could be another disincentive against gaining size.
- **Lack of clarity on cross-border insolvency law:** India has not yet adopted **UNCITRAL (United Nations Commission on International Trade Law) Model Law on Cross-Border Insolvency** and therefore, requires bilateral agreements with individual countries to administer cross-border insolvency proceedings.
  - In June 2018, the Government of India released the suggested draft chapter on cross-border insolvency as an addition to the IBC.

Conclusion

- There is a need to urgently develop a policy framework for distressed asset investors to attract foreign investors in this space. In absence of competing bidders, valuation of assets will be impacted, causing further losses to banks and other creditors.
- A well-designed insolvency & bankruptcy law should differentiate between "financially distressed" firms & "economically distressed" firms.
  - When the present value of the expected profits of a company is less than the total value of the assets of the company, the company is economically distressed. Such a company can be profitably liquidated.
  - In contrast, if a company is not economically distressed but is merely unable to service its debts, it is financially distressed. The assets of such a firm are more valuable if kept together as a functioning unit. Hence, such a unit must be restructured.
- With the passing of 2 years, even as it continues to evolve, the IBC has largely emerged as successful and remains key to solving India's bad loans problem

3.4. DIGITAL ECONOMY

- Currently, India's digital economy **generates about $200 billion** of economic value annually — 8 per cent of India's GVA in 2017–18 — largely from existing digital ecosystem comprising information technology and business process management (IT-BPM), digital communication services (including telecom), e-commerce, domestic electronics manufacturing, digital payments, and direct subsidy transfers.
- India **can create over $1 trillion of economic value from the digital economy in 2025**, with half the opportunity originating in new digital ecosystems that can spring up in diverse sectors, as per a report from Ministry of Electronics and Information Technology, in partnership with McKinsey.
- According to Google and Boston Consulting Group (BCG) titled Digital Payments 2020 study, **digital payments in India will exceed $500 billion by 2020,** up from $50 billion in 2016, which required a comprehensive review of payments sector with an objective to promote access and competition in the payments industry.

3.4.1. DIGITAL PAYMENT SYSTEMS IN INDIA

Why in news?

Recently, the Reserve Bank has released the 'Payment and Settlement Systems in India: Vision 2019 - 2021', with its core theme of 'Empowering Exceptional (E) payment Experience' to achieve "a highly digital and cashlite society".

Background

- The Reserve Bank of India expects the number of digital transactions to increase more than four times to 8,707 crore in December 2021.
- Growth in electronic payments has been substantial with retail payments reflecting large growth in volume terms, while the Systemically Important Financial Market Infrastructures (SIFMIs), such as RTGS system in value terms.
- Further, **new challenges have arisen** requiring new strategies and need to focus on innovation, cyber security, financial inclusion, customer protection and competition.
- The RBI, under powers from the Payment and Settlement Systems Act, 2007, has guided the planned development of payment systems India using its Vision documents. The last document, i.e. Vision 2018 facilitated
    - Continued decrease in the share of paperbased clearing instruments;
    - Consistent growth in individual segments of retail electronic payment systems such as the National Electronic Funds Transfer (NEFT), Immediate Payment Service (IMPS) and card transactions;
    - Increase in registered customer base for mobile banking;
    - Launch of new products like Unified Payments Interface (UPI) and Bharat QR (BQR);
    - Significant growth in acceptance infrastructure;
    - Accelerated use of Aadhaar in payment systems.

Related Information

- The Inter-Ministerial Committee headed by Subhash Chandra Garg submitted draft Payment and Settlement System Bill, 2018, which seeks to setup independent **Payments Regulatory Board (PRB).**
- **Significance of Payment Regulatory Board (PRB)**
    - **Shifting of Power from RBI to PRB**: Bill proposes a major change in the payment industry which seems necessary because it was observed that central banks deal with matters of systematic importance only and their main aim is to promote financial stability.
    - **Improving Efficiency** as PRB will only issue two types of instruments, regulations and orders, thereby, reducing multiplicity of instruments.
    - **Restoring Requisite RBI Power**: Bill provides the RBI with the powers to make a reference to the PRB to consider any matter, which in the opinion of the RBI, was important in the context of monetary policy.
    - **Improving Confidence**: An independent regulator will instill confidence among users and investors.
    - **Improving Financial Inclusion**: A robust Payment regulator will boost digital transactions in India, which is currently close to 90 million.

About Vision 2021 Document

- The Vision 2021 has endeavoured to ensure that India has 'state-of-the-art' payment and settlement systems that are not just safe and secure, but are also efficient, fast and affordable.

- It envisages to achieve the expected outcomes through 36 initiatives, which can be clubber under the following goals
  - **Competition**- in the payment systems landscape, specific thrust areas like creating regulatory sandbox, authorising new players, USSD-based payment services, ensuring inter-regulatory and intra-regulatory co-ordination etc.
  - **Cost effectiveness**- for the customers through initiatives like review of corridors and charges for inbound cross border remittances, inter-operability and building capability to process etc.
  - **Convenience**- by freer access with availability of multiple payment system options anytime-anywhere, setting up a 24x7 helpline, National settlement services for card schemes, widened scope/use of domestic cards etc.
  - **Confidence**- of the customer through the 'no-compromise' approach towards safety of payment systems to address security vulnerabilities, increased coverage of the Cheque Truncation System among others.

Significance

- The Vision 2021 document would act as a catalyst for promoting digital economy and instill confidence among the general public, fintech companies.
- It will help in increasing the digital transactions penetrations especially in the assisted segment in smaller cities and rural India.
- The document has clarity in defining outcomes in terms of scale of digital and overall payments vis a vis GDP, which will help in measuring the impact of work done by all stakeholders.
- With growing competition, industry players will be able to offer services at an optimal cost to their customers and it will also spur innovation in technology and processes that will eventually save time of end consumers.

Other Measures taken by government to promote digital payments

- RBI has removed charges for payments via NEFT and RTGS and asked banks to pass on the benefits to customers.
- Lucky Grahak Yojana and DigiDhan Vyapar Yojana
- BHIM App and QR Codes launched
- **DigiVaart**a has been launched with the express intention of spreading awareness on **DigiDhan**, and also to spread popularity of BHIM's barcode-based merchant payment mode

Expected Outcomes of Vision 2021

- Further decrease in the share of paper-based clearing as a percentage of retail payments.
- Increased deployment of card acceptance infrastructure across the country.
- Reduced demand for cash and achieve reduction in Cash in Circulation (CIC) as a percentage of GDP.
- Further facilitation of mobile-based payment transactions.
- Reduction in pricing of electronic payment systems by at least 100 basis points.
- Security of systems and customer centricity as reflected by decrease in Technical Declines, reduction in Business Declines and improvement in Turn Around Time (TAT) for resolution of customer complaints.
- Enhanced healthy competition in the payments space.

Bali Fintech Agenda

- The International Monetary Fund (IMF) and the World Bank launched the **Bali Fintech Agenda**.
- **Fintech** (financial technology) is used describe new tech that seeks to improve and automate the delivery and use of financial services.
- At its core, fintech is utilized to help companies, business owners and consumers better manage their financial operations, processes and lives by utilizing specialized software and algorithms that are used on computers and, increasingly, smartphones.
- The Bali Fintech Agenda is a set of 12 policy elements established to help member countries harness the benefits and opportunities of rapid advances in financial technology (fintech), while at the same time also managing the risks that arise.
- According to EY's Fintech Adoption Index 2017, India has the second highest fintech adoption rate in the world
- Fintech in India is especially advantageous, since the country boasts of an unrivalled youth demographic which is rapidly growing. Furthermore, smartphone penetration is likely to witness an upsurge - from 53% in 2014 to 64% by 2018.
- The financial services market in India is primarily untapped, with 40% of the population having no association with any bank and more than 80% of the transactions carried out through cash. This represents an opportunity for Fintech start-ups to massively spread their wings in different segments
- **Pillars of Fintech-**
  - Universities and Research Institutions
  - Government and Regulators
  - Investors
  - Financial Institutions
  - Incubators, Accelerators and Innovation Labs
  - Tech Vendors
  - Users
  - Startups

Way Forward

In order to have a coordinated approach towards regulation, the RBI shall engage with the other sectoral regulators — Securities and Exchange Board of India, Insurance Regulatory and Development Authority, Telecom Regulatory Authority of India, etc. to remove friction in regulation and ease system operator and customer comfort.

3.5. OTHER FINANCE RELATED NEWS

3.5.1. INSIDER TRADING

Why in News?

SEBI has laid down mechanism to prevent insider trading on the recommendations of **TK Viswanathan committee**.

Background

- **What is Insider Trading?** It is the buying or selling of a security by someone who has access to material non-public information about the security.
- **Why is it illegal?** As disclosures are often price sensitive, insiders are always in a better position to make bigger trading gains. But since this will be unfair to other investors, and in order to maintain trust and confidence in the market, trading on the basis of unpublished price-sensitive information is illegal.
- **Prohibition of Insider Trading:** In India, **SEBI (Insider Trading) Regulation, 1992** framed under **SEBI Act, 1992** intends to curb and prevent the menace of insider trading in securities. **Companies Act 2013** also prohibits insider trading.
- **Cases of Insider Trading:** The number of insider trading investigations taken up by the market regulator in 2016-17 went up to 34 compared with 12 cases in the previous year.

SEBI's Mechanism to counter Insider Trading

- **Responsibility of Promoters:** It has decided to hold company promoters, irrespective of their shareholding status, responsible for violation of insider trading norms if they possess unpublished price-sensitive information (UPSI) regarding the company without any 'legitimate' purpose.
- **Defining an Insider:** It comprises three elements - The person should be a natural person or legal entity; The person should be connected or deemed to be connected to the company; Acquisition of UPSI by virtue of such connection.
- **Legitimate Purpose:** It has specified that the term "legitimate purpose" will include sharing of the UPSI in the ordinary course of business by an insider, provided that such sharing has not been carried out to evade or circumvent the prohibitions of these regulations.
- **Digital Database:** The board of directors shall ensure that a structured digital database is maintained containing the names of such persons or entities, as the case may be, with whom the information is shared.

Why tackling Insider Trading is a challenging Task?

- **Lack of Manpower:** The Kotak committee report on corporate governance highlighted, SEBI has just one employee for six listed companies, while the US securities market regulator, Securities and Exchange Commission, has about one employee for every listed company.
- **Evolving Technology:** The other problem is that evolving technology and modern means of communication are difficult to track. This only raises the level of complexity for the regulator in tracking insider trading cases.
- **Lax Implementation:** There is difference between rules on paper and reality on the ground which may affect investor confidence

3.5.2. CREDIT RATING AGENCIES

Why in News?

SEBI has **tightened disclosure** norms for credit rating agencies (CRAs) after they failed to warn investors on time about the deteriorating credit profile of Infrastructure Leasing and Financial Services Ltd (IL&FS) which underwent a crisis recently.

More About News?

- The rating agencies will now **need to disclose the liquidity position of the company** being rated and also check for **asset-liability mismatch**. This would **lead to timely availability of information about the company**. This would include parameters such as: Liquid investments or cash balances, Liquidity coverage ratio, Access to unutilized credit lines and adequacy of cash flows for servicing debt obligation.
- CRAs would also need to **disclose the source and rationale if the company is expecting additional funds** to deal with its debt.
- In order to **promote transparency** and to enable the market to best judge the performance of the ratings, the CRA **should publish information about the historical average rating transition rates** across various rating categories, so that investors can understand the historical performance of the ratings assigned by the CRAs. The transition rate indicates the number of instances when credit ratings have changed over a specified period.

Issues with Credit Rating Agencies

- **Conflict of interest:** The CRA Regulations in India currently recognise only the issuer-pays model, under which, the rating agencies charge issuers of bond and debt instruments a fee for providing a ratings opinion. Thus, this model has an **inbuilt conflict of interest.**
  - Another example of conflict of interest is non-rating services such as risk consulting, funds research and advisory services given to issuers for which ratings have been provided.
- **Rating shopping:** It is the practice of an issuer choosing the rating agency that will either assign the highest rating or that has the most lax criteria for achieving a desired rating. Hence, the system does not permit publishing a rating without the issuer's consent.
- **Less competition:** Credit-rating market in India is oligopolistic, with high barriers to entry. Lack of competition in the market enables CRAs to have longer, well- established relationships with the issuers which can hamper their independence.
- **Poor Rating Quality:** Often ratings are provided on limited information. For e.g. If the issuer decides not to answer some determinant questions, the rating may be principally based on public information. Many rating agencies don't have enough manpower which often leads to poor quality.
- **Independence of the ratings committee:** Over the years, the membership of the ratings committee has shifted from external experts to employees of the ratings agency which has raised concerns about their independence.

Credit rating agencies in India:

- The Securities and Exchange Board of India (Credit Rating Agencies) Regulations, 1999 empower **SEBI** to regulate CRAs operating in India.
- All the credit agencies need to be registered with SEBI in order to operate in India.
- There are seven Credit Rating Agencies registered with SEBI, viz. CRISIL, ICRA, CARE, India Ratings and Research, SMERA, Infomerics and Brickworks.

Importance of CRAs

- They provide retail and institutional investors with **information** that assists them in determining if debtor will be able to meet their obligations.
- They help investors, customers etc. to get an overall idea of the **strength and stability of an organization** and enable them to make informed decisions.
- These agencies also help build **trust between the investors and the governments** by quantifying the level of risk associated with investing in a particular country. For example-Sovereign credit ratings are given to the national governments which highlight a country's economic and political environment.
- CRAs help **strengthening of secondary market** by increasing borrower pool.
- Credit ratings ensure a discipline amongst corporate borrowers due to because of this desire to have a good image.

Related News

- SEBI came up with set of **wider disclosure norms** for the Credit Rating Agencies (CRA).
- It introduced **a "probability of default" mechanism** under which rating agencies have to disclose the probability of default for the issuers they rate by December 2019.
- It also provides for **formulation of Uniform Standard Operating Procedure** for tracking and timely recognition of default.

Suggestions for addressing these challenges

- **Removal of conflict of Interest:** Moving back to the earlier "subscriber pays" model in which investors pay for the ratings can be a possible approach.
- **Role of Regulators**: They should **review their regulations and suitably modify** them to ensure greater objectivity, transparency and credibility in the whole credit rating framework.

- Ministry of Finance should seek a factual report from the concerned regulators regarding the enforcement of the regulations and assess the action taken by the regulators against the CRAs.

* **Increase competition among rating agencies** by lowering threshold for registration for CRA to encourage more entities, particularly start-ups with the requisite capability and expertise. It will help investors to better gauge the performance of credit rating agencies.
* **Improve Quality of Ratings:**
    - SEBI must also assess the predictive ability of the current rating models followed by the agencies. There is a need to invest **in high-tech predictive modelling** techniques.
    - Increased remuneration for manpower to attract the best talent must be ensured.
* **Cursory disclosure of all ratings**: CRAs can be asked to provide briefly in their press release to the **ratings given by other CRAs to the same borrower**. This can help in discouraging "rating shopping".
* **Legal protection for CRAs**: There are instances of Indian CRAs being sued by the company it rates, in a bid to prevent the rating downgrade. The regulator should consider framing laws that allow CRAs to express their rating opinion without fear of being sued.
* **Mandatory Rotation of Rating Agencies** for avoiding negative consequences of long term associations between the issuer and the credit rating agency.
    - It will **help reduce recurrence of major default** cases such as the Infrastructure Leasing & Financial Services (IL&FS) crisis.

4. BANKING AND MONETARY POLICY

Introduction

- The banks are the lifelines of the economy and play a catalytic role in activating and sustaining economic growth, especially, in developing countries like India. Since the 1970s, public sector banks (PSBs) have been in the forefront of mobilizing resources from far-flung rural areas as well as extending banking services in the remotest parts of the country. In recent times, apart from banks, other entities in the non-banking financial companies are also contributing towards some of the key functions of banking sector.
- **Some of the key functions are performed by banking sector include**
  - **Mobilizing and pooling savings** of diverse individuals, overcoming transaction costs and invest in projects that elicit high returns, thereby enabling economic growth.
  - As a provider of capital, financial intermediaries can effectively monitor and influence how firms use **capital and utilize resources more effectively.**
  - It **help mitigate risks associated** with individual firms, industries, countries etc. by investing in a diversified portfolio of innovative projects.
  - It **facilitates transactions in the economy**, by providing the mechanism to make and receive payments.
- **Some of the issues faced by the Banking sector are-**
  - **Poor Asset Quality-** In the last decade, when Indian economy was growing at a hefty pace, the banks overleveraged its lending expecting higher returns. However, the global financial crisis, the government stimulus and bad lending practices led to accumulation of bad assets in the banking sector, especially Public Sector Banks.
  - **Bank Governance** and their capacity to deal with various risks in the economy.
  - **Lack of monetary policy transmission** by the banks to the customers.
  - **Bank Consolidation vs. Bank Diversification** (Niche Banks)

4.1. ASSET QUALITY

4.1.1. DECLINE IN NPAS

Why in news?

Due to various steps taken by Government and RBI, there has been a reduction in NPAs.

More about News

- According to Economic survey 2018-19, the **performance of the banking sector** (domestic operations), and Public Sector Banks in particular, **improved in 2018-19**.
- The Gross Non-Performing Advances (GNPA) ratio of **Scheduled Commercial Banks (SCBs) decreased from 11.5 % to 10.1** % between March 2018 and December 2018 while for **PSBs it declined from 15.5 % to 13.9** % %.
- **Capital to risk-weighted asset ratio (CRAR) of SCBs increased from 13.8 per cent to 14.0 per cent** between March 2018 and December 2018 largely due to improvement of CRAR of Public sector banks (PSBs).
- However, the **GNPA ratio of NBFC sector deteriorated** to 6.5 per cent as in December 2018 from 6.1 per cent in March 2018.

Stressed Assets

It is a broader term and comprises of NPAs, restructured loans and written off assets.

- **Restructured Loans**: Assets/loans which have been restructured by giving a longer duration for repayment, lowering interest or by converting them to equity.
- **Written off Assets**: Assets/loans which aren't counted as dues, but recovery efforts are continued at branch level – done by banks to clean up their balance books.

Non-performing asset (NPA)

It is a loan or advance for which the **principal or interest payment remained overdue for a period of 90 days or more.** In case of Agriculture/Farm Loans, the NPA varies for short duration crop (interest not paid for 2 crop seasons) and long duration crops (interest not paid for 1 Crop season).

Banks are required to classify NPAs further into Substandard, Doubtful & Loss assets.

- **Substandard assets**: Assets which have remained NPA for a period less than or equal to 12 months.
- **Doubtful assets**: Assets which have remained in the substandard category for a period of 12 months
- **Loss assets**: It is considered uncollectible and of such little value that its continuance as a bankable asset is not warranted, although there may be some salvage or recovery value.

Why there has been decrease in NPAs?

- Government has taken comprehensive steps under its **4R's strategy** of
  - **Recognising NPAs transparently**-
    - through **Asset Quality Reviews** and **Joint Lenders' Forum.**
    - Banks are now required to acquire **Legal Entity Identifier (LEI)** number from the borrower and report it to Central Repository of Information on Large Credit.
  - **Resolving and recovering** value from stressed accounts-
    - ✓ New **Insolvency and Bankruptcy Code, 2016 (IBC),** has been enacted, which has provided for the taking over management of the affairs of the corporate debtor at the outset of the corporate insolvency resolution process
    - ✓ Amendment to the **Banking Regulation Act, 1949** to empower the RBI.
    - ✓ Amendment to the **Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002** to make it more effective
    - ✓ **Project Sakshat**: to resolve the problem of NPAs through a market-led approach.
  - **Recapitalising**-
    - Government of India announced recapitalization of PSBs to the tune of **Rs. 2.11 lakh crore** in October 2017, through infusion of capital by the Government and raising of capital by banks from the markets.
    - **Deposits with the banking system**, both demand and time has recorded acceleration in their growth, leading to an **increase** in aggregate deposits by 9.6 percent in 2018-19.
  - **Reforms** in banks and financial ecosystem to ensure a responsible and clean system.
    - ✓ Comprehensive framework for transforming the PSBs under **Mission Indradhanush, 2015.**
    - ✓ Under the **PSB Reforms Agenda**, PSBs have created Stressed Asset Management Verticals to focus attention on recovery and entrusted monitoring of loan accounts of above Rs. 250 crore to specialised monitoring agencies.
    - ✓ **Fugitive Economic Offenders Act, 2018**: It has been enacted to deter economic offenders from evading the process of Indian law by remaining outside the jurisdiction of Indian courts.

Reasons for high NPAs

Borrower's side

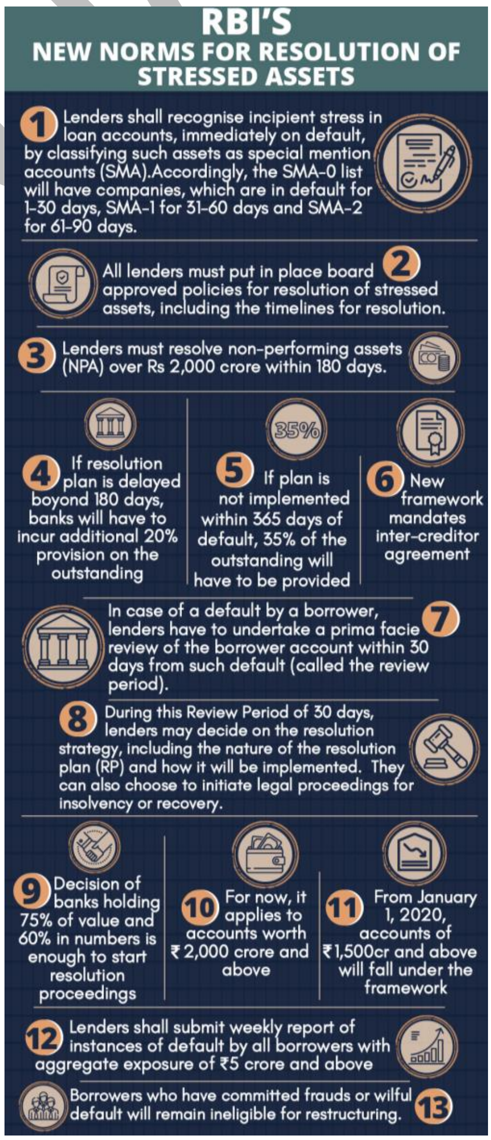
- Domestic economy slowdown - Lack of demand for their products as foreseen by the industrialists
- Wilful default
- Diversion of funds by borrowers for purposes other than mentioned in loan documents.
- Global economy slowdown
- Volatility in prices of raw material and the shortage in availability of power etc. impacts the performance of the corporate sector

Bank's side

- Bad lending practices. Sometimes banks provide loans to borrowers with bad credit history. There is high probability of default in these cases.
- Inadequate Capacity to evaluate projects – poor credit appraisal system
- Absence of regular industrial visits.

Other external factors:

- Economic condition of a region effected by natural calamities
- Ineffective recovery tribunals
- Change in government policies – For example – any government scheme diverting manpower of PSBs for its implementation affecting the regular activities of banks.
- Administrative hurdles – delay in getting permits and other clearances affects the cost of project.



- ✓ With a view to removing the regulatory arbitrage between banks and non-banks, the Reserve Bank has been **aligning** the regulatory and supervisory frameworks for **NBFCs with that of SCBs.**
- ✓ Owing to the sharp deterioration in finances of state-owned banks on the back of rising NPAs, 11 public sector banks were put under **Prompt Corrective Action (PCA)** last year.
- ✓ The **consolidation of Banks** is also seen as a way out of the NPA issue through the "strong" banks absorbing the strain on the books of weaker banks.

Implications of declining NPA

- **On banks**-
  - It increases the **profitability & liquidity** of the banks as annual return on assets comes increases and also the amount given as loan also gets opened which can now be used for some return earning asset otherwise. Banks can grow faster when the availability of credit increases.
  - The **Monetary Policy Transmission** becomes faster for banks to pass on the RBI-induced rate reductions.
  - Banks eases credit to small and medium enterprises (SMEs) that are India's potential for prosperity of an entrepreneurial middle class.
- **On borrowers**- Banks may begin lowering interest rates on some products once Non-performing assets decrease. As a result, the **cost of capital** will decrease, making the different businesses financially viable.
- **On overall economy**
  - Economy will grow as there will be more availability of credit from the security market, which increases employment generation, and development of the country.

How can it be further improved?

- **Managing Risks:** Risk management processes still need substantial improvement in PSBs. Compliance is still not adequate, and cyber risk needs greater attention
- **Improve the process of project evaluation:** and monitoring to lower the risk of project NPAs. Significantly more in-house expertise can be brought for project evaluation.
- **Strengthen the recovery process further:** Both the out of court restructuring process and the bankruptcy process need to be made faster and strengthened.
- **Infusion of Capital:** The government must infuse at one go whatever additional capital is needed to recapitalise banks providing such capital in multiple instalments is not helpful.

4.1.2. NON-BANKING FINANCIAL COMPANIES (NBFCS)

Why in News?

The RBI recently allowed banks to provide partial credit enhancement (PCE) to bonds issued by systemically important non-deposit taking NBFCs registered with the RBI and Housing Finance Companies (HFCs) registered with the National Housing Bank.

More About News

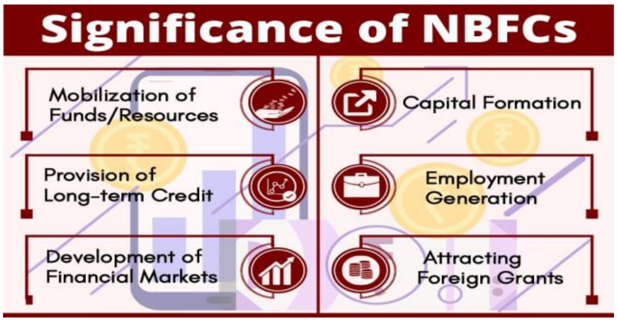
- Credit enhancement means **improving the credit rating of a corporate bond.** For example, if a bond is rated BBB, credit enhancement, which is basically an assurance of repayment by another entity, can

About NBFCs

- A Non-Banking Financial Company (NBFC) is a company registered under the **Companies Act, 1956** engaged in the business of loans and advances, acquisition of shares/stocks/bonds/debentures/securities issued by Government or local authority or other marketable securities of a like nature, leasing, hire-purchase, insurance business, chit business.
- It **does not include** any institution whose principal business is that of agriculture activity, industrial activity, purchase or sale of any goods (other than securities) or providing any services and sale/purchase/construction of immovable property.
- **Systemically important NBFCs:** NBFCs whose asset size is of ₹ 500 cr or more are considered as systemically important NBFCs. **Example**. Power Finance Corporation Limited (PFCL), Rural Electrification Corporation Limited (RECL), IL&FS, etc.
- **Difference between banks & NBFCs:**
  - NBFCs **cannot accept demand deposits** (but some can accept Time deposit and such NBFCs are called Deposit taking NBFC).
  - Unlike banks, **CRR does not apply** on any NBFCs while a **lower SLR** of 15% applies only to Deposit taking NBFC.
  - NBFC do **not form part of the payment and settlement** system and **cannot issue cheques** drawn on itself.
  - NBFCs get license under **Companies Act**, 1956 and Banks under Banking regulation Act.
  - **Deposit insurance facility is not available** to depositors of NBFCs

improve the rating to AA. This is done to provide an additional source of assurance or guarantee to service the bond.

- The move comes at a time when NBFCs and HFCs have requested the government and regulators to ensure that **confidence returns to the market**.

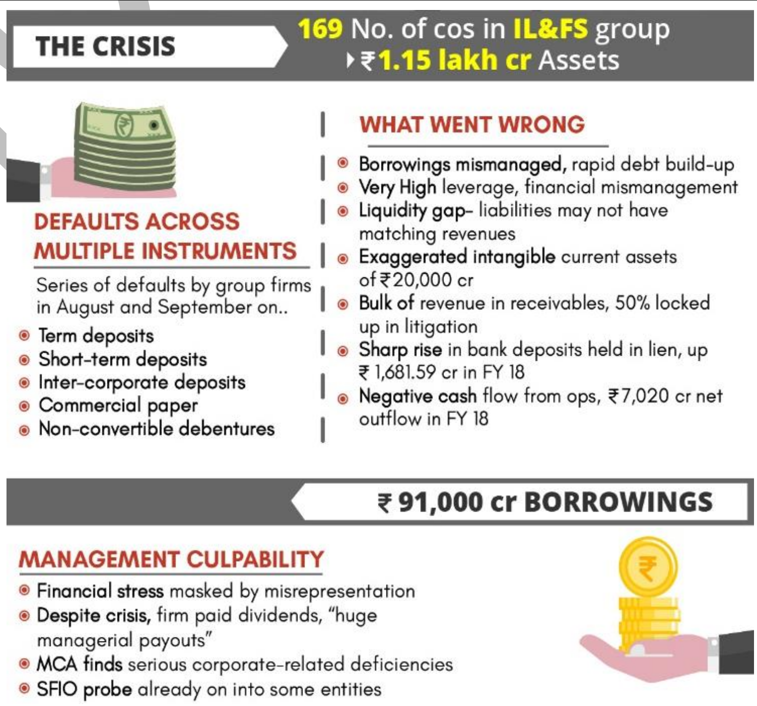


Current problems with NBFCs

- **Multiple regulatory bodies:** RBI doesn't regulate all the NBFC. Other institutions such as NHB (National Housing Bank), SEBI, Insurance Regulatory and Development Authority (IRDAI), etc. are also involved depending on the type of NBFC.
- **Difficulties in access to credit**
  - There is a reversal of interest rate cycle as **interest rates are now going up** both domestically and also in the international market. The RBI has steadily hiked interest rates in the recent months.
  - Another fundamental issue is the **asset-liability mismatch** in the operations of NBFCs as these firms borrow funds from the market — say for 3 or 5 years — and lend for longer tenures — 10 to 15 years. It has led to a situation where the NBFCs are facing a severe liquidity crunch in the short term.
  - The mutual fund is among the biggest fund provider to NBFCs via commercial papers and debentures. These **investors are getting reluctant to lend post the IL&FS crisis.**
- **Riskier Lending Pattern:**
  - Unlike banks, NBFCs are less cautious while lending. For example NBFCs have grown their portfolio of small and micro loans in a big way where there are risks of lack of credit history, scale and historically high NPAs.
  - The unsecure loan segment is also on the rise in the NBFC segment.
- **Cascading effect of Infrastructure Leasing and Financial Services (IL&FS) default**: Default followed by downgrade of IL&FS recently has created a liquidity squeeze for the entire non-banking financial company (NBFC) sector.
- **Delayed Projects:** Many infrastructural projects financed by NBFCs are stalled due to various reasons like delayed statutory approvals, problems of land acquisition, environmental clearance, etc. which has impacted their financial health.

Infrastructure Leasing & Financial Services (IL&FS) Crisis

- Recently an infrastructure financing company, **Infrastructure Leasing & Financial Services (IL&FS),** an NBFC, defaulted on their loan repayment.
- **IL&FS Group** is a vast conglomerate with a **complex corporate structure** that funds infrastructure projects across the world's fastest-growing major economy like Chenani-Nashri road tunnel, India's longest and has raised billions of dollars from the country's corporate debt market.
- IL&FS is a **Systematically Important Non-Deposit Core Investment Company (CIC-ND-SI)** i.e. any crisis at IL&FS would not only impact equity and debt markets but could also stall several infrastructure projects of national importance.
- Many major corporates, banks, mutual funds, insurance companies, etc. such as LIC, HDFC and SBI have stakes in the IL&FS group.



Way Forward for NBFC sector

- **Better Regulatory Regime: The Financial Sector Legislative Reform Commission (FSLRC)** recommendation of creating a body with powers to monitor risk-cutting across sectors should be implemented.
- **Timely Project clearances:** Ensuring timely clearances, especially to infrastructural projects is a must to minimise cost inflation of these projects. Expanding the "Plug and Play" approach to other sectors can be a possible solution.
- **Suggestions for RBI**:
  - RBI must encourage non-banking financial companies to **securitise their assets that can be purchased by banks.**
  - RBI must **revisit lending restrictions placed on banks** under Prompt Corrective Action and consider allowing them lending to NHB.
  - RBI may also **open special window for mutual funds** to get refinance against collateral.
  - A **coordinated and consultative approach** at this point of time to address the various problems of the sector is critical to national economic health and stability.

Recent Steps Taken

- **For IL&FS crisis:**
  - **Change in Management:** The board of IL&FS was superseded with six new directors after the government moved a petition in the NCLT (National Company Law Tribunal) to remove the previous board of directors**.**
  - **Investigation:** Government has also ordered Serious Fraud Investigation Office (SFIO) to investigate into the crisis.
- **For enhancing Liquidity**
  - **Relaxation of the Liquidity Coverage Ratio by 2%:** It means that banks now have an additional 2% of their deposit base freed up for lending
  - **Open Market Operations:** The RBI later also enhanced liquidity into the system by purchasing government bonds from the market.
  - **Relaxing Asset Securitisation Norms:** The RBI has allowed NBFCs to sell or securitise their loan of more than five-year maturity after holding those for six months (Earlier they had to hold these assets for at least one year to do so).

4.2. MONETARY POLICY TRANSMISSION

Why in news?

The State Bank of India Ltd announced the linking of savings bank account deposits and short-term loans to the RBI's repo rate which may ensure faster monetary transmission.

Background

- **Monetary transmission** refers to the process by which a central bank's monetary policy signals (like repo rate) are passed on, through financial system to influence the businesses and households.
- In India, policy rate changes by RBI are not reflected in the base rates of banks regularly. While rate hikes are passed on immediately, but same is not witnessed in rate cuts by the RBI. This shows there is a lag in monetary transmission.
- The available empirical evidence for India suggests that monetary policy actions are felt with a lag of 2-3 quarters on output and with a lag of 3-4 quarters on inflation, and the impact persists for 8-12 quarters.

Concerns associated with ineffective monetary policy transmission

- **RBI is unable to achieve its mandate effectively**- towards regulating various parameters like inflation, growth.
- **Economic situation remains out of control**- whereby country faces job losses, growth in unemployment rates due to stagnating growth.
- **Inflation hurts the marginalized**- as price rise hits at the pocket of poor sections the most. It becomes a failure on the part of a welfare state.
- **Negative signals to the investors**- which are otherwise tempted to invest in India due to its favorable interest eco-system.
- **Uncertainties in business cycle**- where major companies are not able to take decisions with predictable policy cycle.
- **Ineffectiveness of Fiscal Policy**- whereby government incentives like subsidies, interest subventions do not remain attractive as banks do not respond to policy signals.

Reasons for a lag in monetary transmission in India

- **Overdependence on banks**- The Indian financial system remains bank-dominated, and the share of non-bank finance companies (NBFCs) and markets (corporate bonds, commercial paper, equity, etc.) is less. Hence, most public savings are in Bank deposits, reducing the banks' dependency on repo rate.
- **Locking of bank funds**-
  - **Double Financial Repression**- Pressure on banks due to locking of funds in government securities (SLR) and cash reserves (CRR).
  - **Priority Sector Lending**- creates additional burden on banks to lend on a priority basis.
- **Increasing Non Performing Assets**- in bank balance sheets, which impedes the bank's ability to offer lower interest rates.
- **Sub-optimal performance of MCLR system**- As base rate was not flexible enough to transmit monetary policy signals at the desired speed and magnitude, the RBI introduced marginal cost-based lending rate (MCLR) in April 2016. However, as per a report by Janak Raj Committee, the transmission-
  - was uneven across borrowing categories.
  - was asymmetric over monetary policy cycles – higher during the tightening phase and lower during the easing phase – irrespective of the interest rate system.

Marginal Cost of Funds Based Lending Rate (MCLR) System

- The marginal cost of funds based lending rate (MCLR) refers to the minimum interest rate of a bank below which it cannot lend, except in some cases allowed by the RBI. Thus, it is an internal benchmark or reference rate for the bank.
- **Base rate calculation** is based on cost of funds, minimum rate of return, i.e. margin or profit, operating expenses and cost of maintaining cash reserve ratio while the MCLR is based on marginal cost of funds, tenor premium, operating expenses and cost of maintaining cash reserve ratio.
- **Calculation of marginal cost under MCLR**: Marginal cost is charged on the basis of following factors: interest rate for various types of deposits, borrowings and return on net worth. Therefore, MCLR is largely determined by marginal cost of funds and especially by deposit rates and repo rates.

Way Forward

- **Need for shifting to external benchmark based lending rate system**- The internal benchmark-based pricing regimes are not in sync with global practices on pricing of bank loans such as London Inter-Bank Offered Rate (LIBOR).
- Reduce constraints on bank lending through Priority Sector Lending norms.
- Discouraging 'administered interest rate' savings schemes by the government.
- Insolvency process needs to be further strengthened using the IBC, to resolve the NPA problem of banks.

4.3. BANK CONSOLIDATION

Why in News?

The government has decided that Bank of Baroda, Vijaya Bank and Dena Bank shall be "**amalgated**" making the new entity **India's third Largest Bank**.

Background

- **Narasimham committee of 1991** had recommended a restructuring of Indian banks with 3-4 large banks that could be positioned as global banks and 8-10 smaller ones with a national footprint.
- **The P J Nayak committee in 2014** suggested that government should privatise or merge some PSBs.
- In 2017, the government had approved the **"merger" of SBI's** five associate banks and later of the Bharatiya Mahila Bank (BMB) with SBI.
- Last year, the Government had constituted **Alternative Mechanism Panel** headed by the Minister of Finance and Corporate Affairs, Arun Jaitley to look into merger proposals of public sector banks.
  - The proposals received from banks for in-principle approval to formulate schemes of amalgamation will be placed before the Alternative Mechanism.
  - A Report on the proposals cleared by Alternative Mechanism will be sent to the Cabinet every three months.
  - Alternative Mechanism may also direct banks to examine proposals for amalgamation.

Amalgamation vs Merger

- Amalgamation is the combination of one or more companies **into a new entity** (e.g. bank A and bank B combine to form a new bank C).
- In merger one company acquires the other companies. (e.g. bank B acquires bank C and D and eventually only bank B shall exist).

- Alternative Mechanism will receive inputs from Reserve Bank of India (RBI) before according in-principle approval.

Arguments in favour of Consolidation

- **Too many Public Sector Banks (PSBs):** Currently there are **21** PSBs in India which often cannibalise into each other's businesses.
- **Resolving the NPA issue:**
  - Reserve Bank of India expects the gross NPA ratio for state-owned banks to rise to 16.3% by March 2019 from 15.6% in March 2018.
  - The consolidation is being seen as a way out of the NPA issue through the "strong" banks absorbing the strain on the books of weaker banks.
- **Increase in business:** Consolidation will lead to **substantial rise in customer base** and **market reach** along with offering **more services or products to customers**.
- **Global banks:** The consolidation will help create a globally stronger and competitive financial institutions. Currently Indian banks are small when compared with their global peers.
- **Cost cutting:** Consolidation can lead to reduced operating costs for public sector banks as:
  - All duplicate operations and redundancies are rationalised (e.g. shifting and closure of many overlapping branches especially in urban areas).
  - Excessive manpower can be shed off in the long run.
- **Enhanced geographical reach:** For example, Vijaya Bank has strength in the South while Bank of Baroda and Dena Bank had a stronger base in Western India. That would mean wider access for both the proposed new entity and its customers.
- **Greater capital and liquidity:**
  - Merger will lead to a bigger capital base and higher liquidity which will help in meeting the norms under BASEL III.
  - It will also reduce the government's burden of recapitalising the public sector banks time and again.
- **Enhanced human resource:** Merger can lead to availability of a bigger scale of expertise and that helps in minimising the scope of inefficiency which is more common in small banks.
- **Employee welfare:**
  - The merger **will not cause any job loss** in any of these banks and no employee of the banks would have service conditions that are adverse to their present one.
  - The **disparity in wages** for bank staff members will get reduced and service conditions would become uniform.

Arguments against consolidation

- **Setback to corporate governance perspective**:
  - The merger sends out a poor signal of a dominant shareholder (the government) dictating decisions that impact the minority shareholders.
  - Forced mergers of the stronger banks with the weaker banks tend take a toll on the operations of the strong banks. For example: Bank of Baroda's shares took a nosedive in wake of the announcement.
- **Meaningless without implementing governance reforms**: The new entity will face similar problems unless significant reforms take place in the overall functioning of public sector banks. Merger could only give a temporary relief but not real remedies to problems like bad loans and bad governance in public sector banks.
- **Setback to financial inclusion:** Consolidation may lead to large scale shutting down of overlapping branches of the entities being merged. Many banks have a regional audience to cater to and merger destroys the idea of decentralisation.
- **Systemic risks:** There is a global consensus that banks that are "too big to fail" are sources of serious risk to financial stability and consolidation might lead to such a scenario.
- **Protests:** Addressing the concerns of unions and shareholders can prove to be a major roadblock.
- **Varying work culture:** Aligning contrasting HR practices will also pose a challenge to the new management.
- **Harmonization of Technology**: It is a big challenge as various banks are currently operating on different technology platforms.

Way Forward

- **Clear rationale**:
  - The consolidation process among banks should be driven primarily by synergies, efficiency, cost saving, and economies of scale.
  - It is essential to evaluate the merger of banks by assessing the benefits such as cost rationalization, additional business, etc. against the likely future costs.
- **Non-Imposition:**
  - Mergers must happen on commercial considerations and must not be politically imposed.
  - While PSBs are promoted by the government, they are run by their respective professional boards, which should take such decisions.
- **Twin-fold Governance reforms:**
  - Independence from political interference
  - More regulatory power to RBI over PSBs
- **Creating a healthy entity:** It should be ensured that these mergers do not create an entity that is weaker than the original pre-merger strong bank.
- **Training for HR: H**uman resource from the
- smaller bank should undergo training programs to get acquainted with the new processes, technology and environment.
- **Allow "non risky" failures**: Failures are the essence of free market so sometimes we also need measures that allow banks to fail safely without causing systemic shocks.

4.4. DIFFERENTIAL BANKS/ NICHE BANKS

4.4.1. SMALL FINANCE BANKS

Why in News?

Recent data from the Reserve Bank of India (RBI) shows that the small finance bank sector has been seeing remarkable growth in **credit disbursement as well as deposits.**

About Small Finance Banks (SFBs)

- These are **private financial institution** for the objective of financial inclusion without any restriction in the area of operations, unlike the Regional Rural Banks or Local Area Banks.
- They can provide basic banking services like **accepting deposits** and **lending** to the unbanked sections such as **small farmers, micro business enterprises, micro and small industries** and **unorganised sector entities**.
- Some of the **operational Small Finance Banks** in India are: Ujjivan SFB, Janalakshmi SFB, Equitas SFB, AU SFB, and Capital SFB.
- They were proposed by the **Nachiket Mor Committee of RBI,**

	Payment Banks	Small Finance Banks
Who can promote	Prepaid card issuers, telecom companies, NBFCs, Business correspondents, Supermarket chains, Corporates, Realty sector Co-ops and PSUs	Individuals/ professionals with 10 years experience in finance, NBFCs, microfinance cos, local area banks
What they must do	○ Have a minimum capital of Rs. 100 cr ○ Maintain 75% of deposits in govt. bonds ○ Maintain 25% of deposits in other banks ○ Have at least 26% investment by Indians ○ Get listed if net worth crosses Rs 500 cr ○ Have 25% of branches in unbanked areas ○ Be fully networked and technology driven ○ Have Rs 1 lakh cap for deposits in one a/c	○ Have a minimum capital of Rs.100 cr ○ Extend 75% of loans to priority sector ○ Have 25% of branches in unbanked areas ○ Maintain reserve requirements ○ Cap loans to individuals and groups at 10% and 15% of net worth ○ Have a business correspondent network
What they can do	○ Offer internet banking ○ Sell mutual funds, insurance, pensions ○ Offer bill payment service for customers ○ Have ATMs and business correspondents ○ Can function as BC of another bank	○ Sell FOREX to customers ○ Sell mutual funds, insurance, pensions ○ Can convert into a full-fledged bank ○ Expand across the country ○ Transform into a full fledged bank, but only after RBI's approval.
What they can't do	○ Offer credit cards ○ Extend loans ○ Handle cross-border remittances ○ Accept NRI deposits	○ Extend large loans ○ Float subsidiaries ○ Cannot deal in sophisticated financial products

as one of the **differentiated banking system** for credit outreach and announced in the **annual Budget of 2014.**

- Currently, SFBs constitutes **0.2% of the total deposits** of all scheduled commercial banks and makes up **0.6% of the total lending** undertaken by the scheduled commercial banks in India.

Need for Small Finance Banks

- **Differentiated banking to cater large population:** India has **second-largest unbanked population in the world** where more than **200 million people** do not have a bank account and many rely on **cash or informal financing.** Therefore, SFBs provide access to finance to a large unbanked population.
- **Priority sector lending:** SFBs play a key role in the **priority sector lending** space as their main focus is the **unserved and underserved segment**.
- **Financial inclusion of women:** Most of the Small Finance Banks were earlier **microfinance companies** - to provide loans to women. Now that these have become a bank, female customers can avail **full banking solutions**. Also, through different **CSR initiatives,** Small Finance Banks reach out to women customers and make them understand the need of **financial planning and banking services.**
- **Social Impact:** The SFBs are now looking beyond the simple metric of "income improvement" to other indicators of positive social impact, like **customer employment characteristics, customer distribution between urban and rural markets and women's engagement**. SFBs not only serve to provide banking solutions but **empower** the socio-economic progress of its consumers. RBI states that small banks will act as a **savings vehicle** to these segments of the population.

Regulations for SFBs

- They **cannot set up subsidiaries to undertake non-banking financial service activities.**
- They have Minimum paid-up equity capital requirement of Rs **100 crore**.
- The promoter's **minimum initial contribution** to the paid-up equity capital of such bank shall at least be 40% which can be gradually brought down to 26% within 12 years from the date of commencement of operations.
- 75% of its Adjusted Net Bank Credit (ANBC) should be advanced to the **priority sector as categorized by RBI.**
- It must have **25% of its branches set up in unbanked areas**.
- Maximum loan size to a single person **cannot exceed 10% of total capital funds; cannot exceed 15% in the case of a group.**
- They can undertake **financial services** like distribution of mutual fund units, insurance products, pension products, and so on, but **not without prior approval from the RBI.**
- They will be subject to all prudential norms and regulations of the RBI as applicable to existing commercial banks. For ex: **maintaining cash reserve ratio (CRR) and statutory liquid ratio (SLR)**.
- It can transform into a **full-fledged bank**, but only after RBI's approval.

Differentiated Banks

- They are banking institutions **licensed by the RBI** to provide specific banking services and products.
- Main aim for giving license to these banks is to **promote financial inclusion** and payments.
- Differentiated banks licensing was **launched in 2015**.
- They are of two types-**Payment banks and Small finance banks.**

4.4.2. INDIA POST PAYMENTS BANK (IPPB)

Why in News?

Prime Minister on 1st September **launched the India Post Payments Bank (IPPB)** that offers doorstep banking to customers.

About IPPB

- India Post Payments Bank has been incorporated as a **public sector company under the department of posts, with 100% government equity** and is governed by the Reserve Bank of India.
- It **started operations on 30 January 2017**, by opening two pilot branches one in Jaipur and the other in Ranchi.
- It will focus on providing banking and financial services to people in rural areas, by **linking all the 1.55 lakh post office branches with India Post Payments Bank** services by the end of 2018. This will **create the country's largest banking network** with a direct presence at the village level.
- It will offer a **range of products**—savings and current accounts, money transfer, direct benefit transfer, bill and utility payments, enterprise and merchant payments.
    - It will offer **three types of savings accounts**—regular, digital and basic—at an interest rate of 4% per annum.

- It will provide **doorstep-banking facility** at a charge of Rs 15-35 per transaction. The limit for doorstep banking is ₹ 10,000.
  - It will also provide access to third-party financial services such as **insurance, mutual funds, pension, credit products and forex.**
  - It will not offer any ATM debit card. Instead, it will provide its customers a **QR Code-based biometric card.** The card will have the customer's account number embedded and the customer does not have to remember his/her account number to access the account.
  - IPPB has also partnered with different financial organisations to provide loans, investments and insurance products.

Analysis

There are various issues and challenges facing the IPPB, viz-

- **Charges and restrictions**: There are 80 different charges and restrictions (including charges to get cash delivered at doorstep, transactions, withdrawals and deposits, etc) which could prove to be challenges in its objective of financial inclusion.
- **Striking down of certain provisions of Aadhaar by SC** has made Aadhar based KYC authentication difficult. The last mile rural population may not have other required documents prescribed by RBI to become part of the formal financial ecosystem
- **Promoting IPPB as well as Maintaining balance with DoP work by staff:** It needs to be ensured that the work of Department of Posts (DoP) does not get affected by IPPB-related activities. Also, DoP staff needs to be trained in digital operations. For this, they can be associated with the centrally sponsored schemes under Digital India Programme such as NDLM/PMDISHA.
- **Limited manpower in post offices**- Clients might find it difficult to withdraw cash from rural post offices because these are managed by one or two people, who are unlikely to have a lot of money with them.
- **Limited accessibility**- IPPB is **unable to offer ATM cards yet**. As a result clients can't use the united payments interface service.
- **Competition from Private Payment Banks** such as Aditya Birla, Airtel, Jio and Paytm Payment Banks. For eg- there is a need to **review the interest rate of 4%** on savings account which is on a lower side as compared to other Payment Banks
- **Technical Issues**- It's necessary that the customer's fingerprints match the UIDAI database for each transaction. The problem is that the UIDAI told the Supreme Court that it can't ensure 100 per cent biometric matching.
- **Limited appeal- For Urban customers** who have easy access to private banks offering purely digital accounts with more services, interest rates of up to 6 per cent and latest technologies like UPI.
  - Even in rural areas, it is unlikely to make much sense since Jan Dhan Yojana has already provided zero balance bank accounts with RuPay debit cards with full-scale banks.
- **Bad health of postal department**- Department of posts isn't in good health as its deficit doubled in the year 2016-17 and only 55 post offices have been added in the country in the last five years.
- **Sustenance issue:** Since IPPB cannot lend or issue credit cards, the only source of its income would be the

Performance of Payment Banks

- Various payment banks including Aditya Birla Payments Bank (ABPB), Vodafone m-Pesa have closed their operations, citing unanticipated developments in the business landscape that have made the economic model unviable.
- As of now, only 4-PBs are operational out of the 11 licensed players.
- In a recently released report by the RBI entitled **'Trend And Progress Of Banking In India 2017-18'**, the central bank noted that the consolidated balance sheet of payments banks showed net losses during 2016-17 and 2017-18.
- PBs **face stringent regulations on both asset and liability side.** On the asset side, PBs face a blanket ban on any type of lending. On the liability side too, they cannot accept deposits higher than Rs. 1 lakh. Besides, capital requirement is quite steep at 15% capital to risk weighted assets ratio.
- The losses of payments banks **are attributed to high operating expenses as large capital expenditures** had to be incurred in setting up initial infrastructure. On the other hand, margins are small and without economies of scale, these banks find it difficult to survive.
- Payment bank agents report receiving **limited training on the features of the product,** terms and conditions and its benefits.
- **Low levels of awareness** in both the last mile customers and the agents about the product.
- The Payment Bank model to become a success requires both the universal banks and telecom companies to work together having strong infrastructure, deep pockets and network in place.

transaction fee and not interest spread, hence sustenance issues will persist unless it provides its services efficiently, at lower cost.

However, despite these challenges there is also a need to understand various advantages of establishing IPPB-

- Department of Posts and IPPB will need to work in tandem to take the benefits of government schemes and financial services that are not easily available to the marginalized population in urban and rural areas alike. The objective of IPPB will be public service rather than promoting commercial interests.
- While many other banks and financial institutions are working on the same theme, the USP of IPPB will be its ability to ease access and handhold the adoption of new age banking and payments instruments among citizen of all walks of life through the delivery by postmen and Grameen Dak sevaks, savings agents and other franchisees who will take banking to door steps. IPPB thus aspires to the most accessible, affordable and trusted bank for the common man with the motto - **"No customer is too small, no transaction too insignificant, and no deposit too little".**
- If it succeeds, the new payments bank could usher in a new era of rapid financial inclusion across rural India.

5. EXTERNAL SECTOR

5.1. CAPITAL ACCOUNT LIBERALISATION

Why in news?

Recently, RBI's Deputy Governor has argued in favour of revisiting India's policies with respect to Capital Account Liberalisation.

Present Capital Controls in Indian Economy

- Capital control represents any measure taken by a government, central bank or other regulatory bodies to limit the flow of foreign capital in and out of the domestic economy.
- Some of the controls used presently are-
    - Cap on total FPIs in domestic securities with separate limits on different kinds of them.
    - Cap on External Commercial Borrowings (ECBs) and Masala Bonds together.
    - Restrictions on investors by their horizon of investment, such as, Insurance firms, Endowments and Pension Funds etc.
    - Restrictions on maturity of the underlying investment.
    - Restrictions to ensure that only relatively high credit quality borrowers tap into ECBs.

About Capital Account Liberalisation

- **Foreign exchange transactions** are broadly classified into two types: Current account transactions and Capital account transactions.
    - The **Current Account** represents a country's current transactions including exports, imports, interest payments, private remittances and transfers.
    - The **Capital Account** records the net change of assets and liabilities which include external lending and borrowing, foreign currency deposits of banks, external bonds issued by the Government of India, Foreign Direct Investment (FDI), Foreign Portfolio Investments in India (FPI) etc.
- **Currency convertibility** refers the ease with which a country's currency can be converted into gold or another currency in global exchanges. It indicates the extent to which the regulations allow inflow and outflow of capital to and from the country. Thus, for-
    - **Current Account-** Indian rupee can be converted to any foreign currency at existing market rates for trade purposes for any amount.
    - **Capital Account-** It means that ease with which, the foreign investors will be able to buy Indian assets such as bonds, equity and Indian citizens will be able to buy foreign financial assets.
- In the early nineties, India's foreign exchange reserves were so low that these were **not enough to pay for a few weeks of imports.** Hence, India initiated reforms in foreign transactions and in 1994, India allowed **full current account convertibility** in 1994. However, **capital account transactions** were not made fully convertible.
- Since, the last decade, the government and the central bank have been exploring ways and trajectory in which fuller capital account convertibility could be achieved.

Committees on Capital Account Convertibility (1997, 2006)

- The Reserve Bank of India setup committees on capital account convertibility under the chairmanship of S.S. Tarapore in 1997 and 2006 respectively.
- The committee had supported the idea of full convertibility in the capital account. It recommended this to be done in a phased manner and subject to certain preconditions.
- **Some pre-conditions are-**
    - Fiscal Stability- low fiscal deficit
    - Price Stability- low inflation
    - Stability of financial institutions and markets
    - Low Non-Performing Assets

Arguments in favour of Capital Account Liberalisation

- **Bring in financial efficiency-** An open capital account could bring with it greater specialisation and innovation by exposing the financial sector to global competition.
- **Can attract larger foreign capital-** where external capital can supplement the domestic saving in the effort to mobilize resources for welfare and infrastructure.
- **Increase the choices for investments-** Residents get the opportunity to base their investment and consumption decisions on world interest rates and world prices for tradeables, which could enhance their interests and welfare.
- **Improves competitive discipline-** By offering the opportunity of using the world market to diversify portfolios, an open capital account permits both savers and investors to protect the real value of their assets through risk reduction.

- **Helps complement current account-** Capital controls are not very effective, particularly when current account is convertible, as current account transactions create channels for disguised capital flows.
- **Changed global scenario-** Capital controls are there to insulate domestic financial conditions from external financial developments. The influence of external financial conditions, however, has been increasing over the years even in countries with extensive capital controls and because the costs of evading the controls have declined and the attractiveness of holding assets in offshore markets have increased, **capital controls are increasingly becoming ineffective**.

Arguments against Capital Account Liberalisation

- **Could lead to the export of domestic savings**- which can further erode the capacity of state to finance the national imperatives.
- **Could lead to greater tax avoidance**- It would weaken the ability of the authorities to tax domestic financial activities, income and wealth.
- **Could expose the economy to greater macroeconomic instability**- arising from the volatility of short-term capital movements, the risk of large capital outflows and associated negative externalities.
- **May lead to ineffective monetary policy**- due to speculative short-term movements in the interest rates, leading to other spiraling effects.
- Due to higher capital inflows following capital convertibility, the appreciating real exchange rate would **divert resources from tradable to non-tradable sectors** (like construction, housing, hotels and tourism etc.) and this would happen in the face of rising external liabilities (**"Dutch disease effect"**).
- **Could lead to financial bubbles**- especially through irrational exuberance of investment in real estate and equity market financed by unbridled foreign borrowing.

Way Forward

- Given the trade-off between **growth/efficiency and stability** associated with capital flows, India's preference has strongly been in **favour of avoidance of instability**. Such an approach has imparted stability not only to the financial system but also to the overall growth process. The relative weights to efficiency and stability need to be **constantly reviewed** in the view of contemporary developments.
- While realizing that the impulses of growth could be supplemented with foreign capital, it is imperative to ensure that liberalisation of the capital account responds to the requirement of the economy in an **appropriate, gradual and cautious manner**.

5.2. CURRENT ACCOUNT DEFICIT

Why in News?

To contain the widening current account deficit (CAD) and check the fall of the rupee, the government recently announced specific steps to attract dollars and address volatility in the financial markets.

Background

- Though within reasonable levels, CAD is projected at **2.4% of GDP** in 2018-19, up from **1.8% in 2017-18**.
- The widening of the current account deficit has been driven by a **deterioration of trade deficit** from 6.0 per cent of GDP to 6.7 per cent across the two years. **Rise in crude prices** and a **decline in the growth of merchandize exports** have led to the deterioration of trade deficit.
- However, the acceleration in the growth of remittances has offset the deterioration of the current account deficit.

Steps taken by Government to improve Current Account Deficit

Government has taken steps particularly towards attracting more dollars and enhancing exports.

- **Steps taken to attract dollars**
  - Enabling more companies to raise External Commercial Borrowings (ECBs).
  - Removal of exposure limit of 20% of FPI's corporate bond portfolio to a single corporate group.
  - Masala bonds issued in 2018-19 exempt from withholding tax.
- **Recapitalization of EXIM Bank**
  - Recently, cabinet approved **recapitalisation** of **Export-Import Bank of India (Exim Bank).**
  - Further, cabinet also approved an **increase in the bank's authorised capital** from Rs. 10,000 crore to Rs. 20,000 crore.

- **Advantage:** It will enable bank to augment capital adequacy and support Indian exports with enhanced ability.

- **Swap Facility provided**
  - The Reserve Bank of India (RBI) has introduced a **$5-billion dollar-rupee swap facility** for the banks to facilitate **permanent liquidity support**.
  - Under the swap, a bank would sell US dollars to the RBI and simultaneously agree to buy the same amount of US dollars at the end of the swap period.
  - **Benefits of the Swap Facility**
    - ✓ **Reduce interest by banks-** with improved liquidity condition with the banks, especially after constrained balance sheets due to double financial repression. This will help customers with cheap loans for homes, cars etc.
    - ✓ **Increase RBI's Foreign Exchange Reserves-** the auction will help boost it by another $5 billion to the current $400bn corpus. This further improves India's capacity in dealing with hot money outflow and balance of payment crisis.
    - ✓ **Control appreciation of Rupee-** as there will be increased supply of Rupee. This will help Indian exporters.
    - ✓ **Reduce financial stress on NBFCs-** Lending from the Non-Banking Financial Companies may also increase.

About Masala Bonds

Masala bonds are rupee-denominated debt securities issued outside India by Indian companies.

The bonds are directly pegged to the Indian currency. So, investors directly take the currency risk or exchange rate risks.

Withholding Tax

It is an amount that an employer withholds from employees' wages and pays directly to the government. It also is a tax levied on income (interest and dividends) from securities owned by a non-resident as well as other income paid to non-residents of a country.

Exim Bank of India

- It was established in 1982 under an Act of Parliament as the apex financial institution for financing, facilitating and **promoting India's international trade**.
- The Bank primarily **lends for exports from India** including supporting overseas buyers and Indian suppliers for export of developmental and infrastructure projects, equipment, goods and services from India.

Important EXIM Bank Initiatives

- **Concessional Finance Scheme (CFS)** - Under it, government has been supporting Indian Entities bidding for strategically important infrastructure projects abroad.
- **GRID (Grass Roots Initiative and Development) Initiative –** This includes **financial support** to promote grassroots initiatives, particularly the ones with export potential and help them realise remunerative return on their produce and facilitate exports from these units.

Role of Exim in Foreign Policy and Trade

- **Improve Foreign Trade:** Bank provides assistance in various financial, marketing and technical aspects by engaging into various programs and services in the interests of Indian exporters, commercial banks, financial institutions to promote foreign trade in the country.
- **Increasing India's Sphere of Influence**: Exim Bank has 233 Line of Credit (LOCs) in place at present, covering 62 countries in Africa, Asia, Latin America and the CIS, with credit commitments of around $22.86 billion, available for financing exports from India.
- **Crucial role in**- Integrating ASEAN in India's Act East Policy by setting up Project Development Fund, Cooperation with BRICS Bank through a MoU on general cooperation with the New Development Bank (NDB).

6. CORPORATE GOVERNANCE

6.1. SHELL COMPANIES

Why in news?

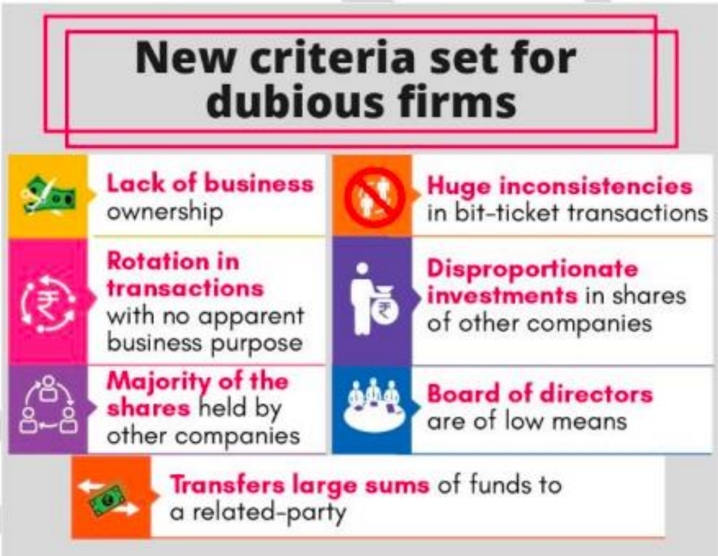
Government has identified and denotified 4 lakh shell companies amidst a government crackdown on money laundering and tax evasion.

Background

- In India Shell companies are **not defined under Companies Act, 2013 or any other legislation.** However, some laws can help curbing illegal activities such as money laundering and can indirectly be used to target shell companies — Benami Transaction (Prohibition) Amendment Act 2016; The Prevention of Money Laundering Act 2002 and The Companies Act, 2013 etc.
- Under Section 248 of the Companies Act, the Registrar of Companies (RoC) can remove a company from its records if it fails to commence business within a year of its incorporation, or has not carried out any operation for three years.
- A Task Force was constituted in 2017 for effectively tackling the malpractices by shell companies in a comprehensive manner. It gave following recommendations-
    - It **listed certain key parameters** to determine if a company has been created to launder money or exploit regulatory arbitrage (See Picture).
    - Ministry of Corporate Affairs must look into the filings of financial statements of companies which had been misused to channel unaccounted cash after demonetisation.
    - Keeping a watch on companies with abnormal increase or decrease in debts, or more than 10 per cent of bad debts written off, and the increase in investment in partnership firms by 100 per cent or more.

Shell Companies

- Shell companies typically refer to companies without active business operations or significant assets.
- Task force has explained that a typical shell firm is incorporated with a standard memorandum or articles of associations. It has inactive shareholders and directors, and is **left dormant.** It is created for the purpose of being palmed off later.
- After the sale transaction, inactive shareholders usually transfer their shares to the buyer and the so-called directors resign or flee.



Other Government Measures to tackle shell companies

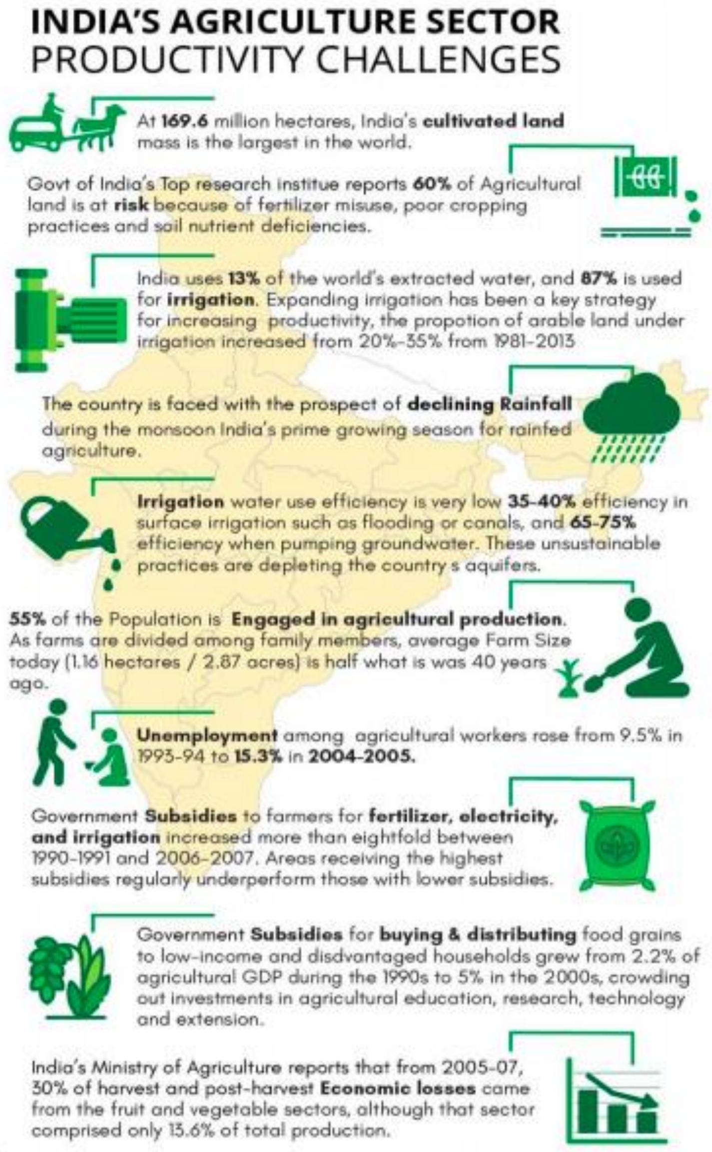
- **Serious Fraud Investigation Office** under the Ministry of Corporate Affairs has **prepared comprehensive digital database of shell companies** that were identified by various law enforcement agencies.
- **Information sharing mechanism** between various law enforcement agencies is implemented under the Regional Economic Intelligence Council (REIC) and Central Economic Intelligence Bureau (CEIB) forums.
- **Issue with Auditors**: Role of auditors has also come under the scanner for alleged connivance in facilitating illegal transactions and not raising the red flag when such things came to the fore.
    - The MCA is examining the recommendations of the 3-member expert panel on various **issues related to audit firms** headed by TERI chairman Ashok Chawla.
- Government has removed the exemption under Section 276CC of the Income Tax Act through Budget 2018-19. It provided that if a person with tax liability more than Rs. 3000 wilfully fails to furnish the return of income in due time, he shall be punishable with imprisonment and fine. The provision was being misused by around 3 lakh inactive companies showing nil income.

7. AGRICULTURE AND ALLIED SECTOR

Introduction

Agriculture (inclusive of animal husbandry, forestry and fishing) is central to the nutrition needs of India and remains the largest sector of India's economy as a source of employment and accounts for 17% of India's GDP.

Some major issue pertaining to Indian Agriculture are:



- **Low Agricultural Productivity**: India's crop yields are lower than those in the US, Europe and China.
- **Policy Issues**: There has been an absence of policy coherence between the Centre and states on the interlinked issues of agriculture.
- **Inefficient Agricultural Marketing**: In the absence of sound marketing facilities, farmers have to depend upon middlemen for the disposal of their farm produce which is sold at throw-away prices.
  - Agricultural Produce Market Committee (APMC) Act has also allowed the cartelization of traders that keeps farm-gate prices low.
- **Input Challenges**: Rise in input cost has led to decline in crop income over the years, which has resulted in the low productivity and purchasing power of farmers.
- **Inefficient MSP structure**: Only 6% farmers get the benefit of MSP and remaining 94% are dependent on the markets.
- **Large number of farmers want to quit**- The survey of 5,000 farm households across 18 states says that 76% farmers would prefer to do some work other than farming.
- **Climate Change**: Higher frequency of extreme weather events are adversely affecting agricultural production through soil erosion, pest attack, crop failure etc.
- **Lack of enabling infrastructure along the value chain**: including cold storage, warehouses, and agro-processing—has not developed in corresponding speed with rising agricultural production leading to food wastage, poor price discovery for farmer, distress sale of product etc
- **Low investment in Research & Development**: Less than 1% of the Agricultural GDP in India is spent on research.
- **Market Sluggishness**: sharp fall in prices in both domestic and global market, interventionist government policies like restrictions on exports of certain food items like pulses despite surplus supply, ban on futures trading and imposition of stockholding limits, among others are adding to farmers' distress despite bumper crop.
- **Rural Distress & Farmer Suicides:** According to National Crime Records Bureau (NCRB) report (2015), over 8000 farmers and 4500 agricultural labourers have committed suicide.
- **Agricultural NPA's**: According to Reserve Bank of India data, NPAs in agricultural sector rose over 23% from Rs 48,800 crore in 2016 to Rs 60,200 crore in 2017 due to

- Dependence of Monsoon – Farm outputs were heavily affected by successive droughts which has led to harvest losses.
- **Increasing Rural Distress** –Average all-India annual rural wage growth declined from 6.8 to 4.9 % between July and October and the decline is sharper for agricultural than for nonagricultural occupations.
- **Moral Hazard of Farm Loan Waiver** - Expectations of loan waiver prompt farmers to default on loans. Moreover, it has a domino effect such that farmers from different states demand loan waivers.
- **Using Loan Amount for Non-farming Purposes** - Farmers take loans through channels like Kisan Credit Card and using it for other non-farm activity including private consumption.

Suggestions for tackling agricultural distress

Recommendations of Ashok Dalwai Committee on Doubling Famers' Income by 2022

The committee has given reports in 14 volumes and following are the top line recommendations of these-

- **Recognize agriculture in India as an enterprise**- that is based on the principles of profit. Following actions have been recommended-
  - Pursue adoption of **NITI Aayog's Model Land Leasing Act** by all the states and UTs in a time bound manner.
  - Enable farm owners to **transit from the status of cultivators to farm managers** by outsourcing all possible farm operations, so as to achieve both resource use efficiency and effective outcome, besides realising reduced cost of cultivation. Farmers should transact with the service providers as a Group like Village Produce Organisations (VPOs), Farmers Produce Organisations (FPOs) etc.
- **Expand the mandate of agriculture**- from food and nutrition security existing currently-
  - To generate resources as raw materials to feed and support industrial enterprises – chemicals, construction, energy, fibre, food, medicinal, etc.
  - Shift from only farm activities to farm + on-and-off farm activities (primary + secondary agriculture)
- **Water may be treated as the 'determining factor' of production**- rather than considering it as a mere input. Following things should be done-
  - Creation of additional sources of water – an addition of 8 to 9 million hectares under irrigation (AIBP, MGNREGA etc.) by 2022-23
  - Efficient use of water – 2 to 2.5 million hectares under micro-irrigation per year
  - Saving on ground water and its sustainability through recharge
  - Crop alignment based on 'path of least resistance'. It implies in promoting agroclimate based cropping/production system, the best option need not be the one chosen. It can be an option that is more acceptable to the farmers
- **Adopt 'Fork to Farm' approach**- by reversing the 'Farm to Fork' approach now accepted generally in the following manner-
  - Adopt monetisation of produce as the basis for maximising the value capture for the farmers.
  - Maximise monetisation possibilities by upgrading and harmonising the agri-logistics (storage & transportation), agro-processing and marketing.
  - Adopt new market architecture comprising GrAMs, alternate Wholesale markets (APMCs - in private & public sectors) and Export market.
  - Promote Agricultural Value System (AVS) as a link between farms and markets
- **Adopt risk management strategies at all the stages of agriculture-**
  - **Pre-and Post-production stages-**
    - ✓ Replicate Meteorological Advisory Services across the country; on the lines of the technology platform adopted in Karnataka.
    - ✓ Coverage of farming under Pradhan Mantri Fasal Bima Yojana (PMFBY) should become a norm.
  - **Market risks-**
    - ✓ Adopt an institutional mechanism for price & demand forecasting.
    - ✓ Adopt an import-export duty structure, that helps domestic market sentiments to the advantage of farmer-producers.
- **Improve Institutional Arrangement/Overhaul of the Union agriculture minis**try: through steps such as o reorganizing some of the divisions of ministry to bring into focus new aspects like agri-logistics, investments for capital formation, primary processing etc.
  - setting up a three-tier planning and review mechanism through district, state and national level committees

- establishing a national level policy and planning committee to review the policy framework and progress in doubling farmer's incomes, review trade policy, budgetary allocations and status of farmers' welfare.

- **Liberalize the definition of a 'farmer'** to include cultivators, lessee farmers and sharecroppers and developing an online and annually authenticated database to identify a farmer and render him/her eligible to avail benefits of agriculture related support-system of government.

7.1. AGRICULTURAL CENSUS

Why in news?

The 10th Agriculture Census 2015-16 was released by the Agriculture Ministry.

Key Findings of Provisional Agriculture Census 2015-16 vis-à-vis 2010-11 Agri- Census

Description	2015-16	2010-11	Remarks
Total number of operational holdings	146 million	138 million	Increase of 5.33%. (Share of SC- 11.91%, ST-8.72%)
Total operated area	157.14 million HA	159.59 million ha	Decrease of 1.53%.
Average size of operational Holding	1.08 hectares ha	1.15 ha	Declining average land holding size
Share of female operational holders	13.87 %	12.79 %	Rise in female participation
Small and Marginal holdings (0-2 ha)	86.21 %	84.97 %	Increasing fragmentation of land holdings leading to farmer distress among other farming issues
Semi-medium and medium operational holdings (2-10 ha)	13.22 %	14.29%	
Large holdings (10.00 ha & above)	0.57%	0.71%	
Share in Operated Area			
Small and Marginal holdings (0-2 ha)	47.34%	44.31%	• Share of larger land holdings in total cultivated area is declining while smaller holdings on rise. • As per Social groups, share of SC- 8.61%, ST-11.4% • Female share in land holding is rising which is a positive sign
Semi-medium and medium operational holdings (2-10 ha)	43.61%	44.82%	
Large holdings (10.00 ha & above)	9.04%	10.59%	
Females	11.57%	10.36%	

Issue related to land in India are scarcity of Land Resources:

- The figures show **landholdings have doubled in past 45 years** (from 71 million in 1970-71 to 146 million in 2015-16), resulting in decline in average size of farms by more than 50%.
- While farms got more fragmented between 2010-11 and 2015-16, **holdings continue to be inequitably distributed.**

Problems associated with fragmentation of Land holdings

- **Small scale of production:** It inhibits the ability of farmers to reap economies of scale in agricultural operations and invest in mechanisation. It further leads to decline in productivity and thus declining land capability.
- **Low Prices:** Further the small and marginal farmers have low bargaining power, since they have very little marketable surplus and are price takers in the market.
- **Low income:** As per NSSO Survey (2012-13) the median agricultural incomes were about Rs. 19,250 or about Rs 1600 per month in 2012-13.
- **Indebtedness:** As per Economic Survey-2016-17, there is an **inverse relationship** between indebtedness and the size of land holding. In Bihar and West Bengal, more than 80% of agricultural households with marginal landholdings are indebted.
- **Inclusion Issue**: The existence of a large number of small and marginal farmers means it is **challenging for the government's extension arms** to reach them with new technology and farm support schemes.
- Overall it makes farmers **prone to all sort of agricultural risks** including Production risks, Climatic risks, Price risks, Credit risks, Market risks, and Policy risks.

Way Forward

- With **land being a State subject**, States can take specific legal reforms to ease land acquisition process by consulting every stakeholder.
- **Furnish details about usage of acquired land**: People have the right to know about usage of land acquired by government by way of compensation. For e.g.- in Britain, the government has pledged to provide details of ownership, location and intended use for all properties.

Feature of Draft National Land Reforms Policy, 2013

- **National land use plan**: based on information from tehsils, districts, regions and states.
- **Land rights for vulnerable sections** such as SC/STs, women etc.
- **Dispute resolution**: by establishing an authority at the sub district level and a tribunal at state level for land related dispute resolution.
- **Modernisation of Land Records:** Establishing a National Authority for Computerisation of Land Records and State Authorities for Computerisation of Land Records.
- **Monitoring and evaluation:** Establish Land Rights Commission (LRC) at State level to review the progress made by state governments on the realisation of land rights.

- **Comprehensive inventory of land resources and usage patterns:** It should be made with information on the location of each property, its dimensions, legal title, current & planned use etc. to enable effective identification of land usage pattern.
- Early Finalisation of **National Land Reforms Policy**
- **Scale-up the farms:** There are various ways such as land pooling, land leasing and contract farming etc. All this should be done within proper legal mechanism.
    - **Land Pooling** is also known as land readjustment or land reconstitution. It is a land acquisition strategy where ownership rights of privately held land parcels are transferred to an appointed agency, with these land parcels being pooled as a result. The agency uses some of the pooled land for infrastructure development and sale, while the rights to new parcels in the pooled land are transferred back to the original landowners in some proportion to their original property.
- **Use of surplus land**: It should be utilised to meet the growing demands for services such as water and waste disposal, housing and transportation projects etc. and land intended for future use should be rented out, through a transparent bidding process, till such time it is needed.
- **Model Land Leasing Law:** NITI Aayog has formulated a Model Agricultural Land Leasing Act, 2016 to both recognize the rights of the tenant and safeguard interest of landowners.

7.2. AGRICULTURAL INPUTS

7.2.1. PM KISAN SAMMAN NIDHI

Why in news?

In the Interim Budget 2019-20, the Union Government has launched the **Pradhan Mantri Kisan Samman Nidhi (PM-KISAN).**

About PM-KISAN scheme

- **Objective:**
    - To provide income support to all farmer families having cultivable land.
    - To **supplement the financial needs** of the farmers in procuring various inputs to ensure proper crop health and appropriate yields, commensurate with the anticipated farm income.
- **Benefits**: Under the scheme, financial benefit of ₹ 6,000 per year will be provided to all 14.5 crore farmers in the country, irrespective of the size of their landholding.
- **Responsibility of identifying** the landholder farmer family eligible for benefit under the scheme shall be of the **State/UT Government.**
- The lists of eligible beneficiaries would be **published at the village level** to ensure transparency.
- **Exclusions**: Certain categories of beneficiaries of **higher economic status** such as institutional land holders, former and present holder of constitutional posts, persons who paid income tax in last assessment year etc. shall not be eligible for benefit under the scheme.
    - For the purpose of exclusion **State/UT Government can certify** the eligibility of the beneficiary based on **self-declaration** by the beneficiaries.
- A **dedicated PM Kisan Portal** will be launched for implementation of the scheme.
- This is a **Central Sector Scheme** and will be **funded fully by the Government of India.**

Benefits of PM-KISAN

- For the first time, an attempt has been made to **transfer income directly to farmers without using price** (of either inputs or output) as a policy tool. Earlier, the focus has mainly been on provision of inputs at lower price (input subsidies) and provision of a higher output price (MSP).
- Since benefits are not linked to production of any crop, the **resultant supply-demand imbalance would be minimal**, unlike in the case of MSPs.
- Many **farmers still depend on informal sources** (local arhatiyas, moneylenders etc.) **for credit**. There are substantial delays in payment by procurement centres (e.g. in case of sugarcane), which leads to distress selling. Providing **assured supplemental income** to the vulnerable farmer families would help them meet their emergent needs especially before the harvest season.
- It would **improve the credit uptake** and **boost rural consumption demand.**
- The **cash transfers have greater efficiency** than loan waivers & subsidies, as they enable poor households to directly purchase required goods & services as well as enhance their market choices.
- With the support of a minimum income, **youths from farm households** may be **inspired to start enterprises** or take higher training or look for higher paying non-farm jobs.

Issues in conception & implementation

- **Insufficient Amount:** Annual direct income transfer (DIT) under PM-KISAN would be only about 5-8% of their existing income levels. Also, it is less in comparison to schemes rolled out in Telangana (**Rythu Bandhu**) and Odisha (**KALIA**).
- **Beneficiary selection:** Under this scheme, **family is being defined as a unit**, while most other government schemes use household (group of people living together using common kitchen) as a unit. The **re-classification** might be an administrative challenge.
  - It is unclear if beneficiary farmers, who wish to lease their lands to tenant farmers or keep their lands fallow for some time, are eligible to receive cash benefits.
- **Coverage:** The scheme **does not include landless farmers** - tenants, sharecroppers etc.
  - Many Adivasi communities also cultivate land as **community farmers** & without individual rights, and may be left out of the scheme, although they are among the most vulnerable.
- **Poor maintenance of land records:** In most parts of the country, **land records are not regularly updated**, especially in case of inherited land, which may lead to exclusion of beneficiaries.
  - Many states (e.g. Jharkhand, Bihar, Gujarat & Tamil Nadu) have still **not digitized land records** under Digital India Land Records Modernization Programme.
- **DBT related issues:** Direct cash transfer in accounts has previously met (like in MNREGA) with **delays in disbursing wages**. Also, rural banking infrastructure has poor outreach & lacks last mile connectivity.
  - Cash transfers can be **eroded by local price increases**, even if they are indexed to the general price level.
- **Impact on Agriculture**: Lure of cash benefits may further **induce fragmentation** of family-owned land among members.

Way Forward

- **Address the lacunae in the existing scheme** like exclusion of landless farmers & create adequate institutional infrastructure for easy identification of beneficiaries and land record reconciliation.
- Today, agriculture in India faces diverse set of problems, such as Punjab faces scarcity of water, Bihar faces the challenge of poor supply chains and lack of infrastructure. Rather than merely focussing on income support, the policy makers need to focus on **finding synergies and creating enabling environment** to deal with these challenges in a holistic manner.
- There is a need for **comprehensive social security package for farmers**, which includes health insurance as well. The KALIA scheme, which includes a life insurance cover & additional personal accident coverage of Rs 2 lakh, is a good example in this regard.
- This could pave a way for the **introduction of minimum basic income (MBI) for farmers** in future.

7.2.2. PRADHAN MANTRI ANNADATA AAY SANRAKSHAN ABHIYAN (PM-AASHA)

Why in News?

The Union Cabinet approved a new umbrella scheme – ‘Pradhan Mantri Annadata Aay SanraksHan Abhiyan’.

Background

- **Minimum Support Price (MSP) system suffers from various shortfalls** such as limited geographical reach and crop coverage. It works well only where there was direct procurement by industries.
- Also, prices of key agricultural commodities have fallen below their MSP due to which there is increasing farmer unrest across the country.
- PM-AASHA scheme thus aims to **plug the gaps in procurement system**, address issues in MSP system and give better returns to farmers.

About the scheme

It has **three components** complementing the existing schemes of the Department of Food and Public Distribution for procurement of paddy, wheat and other cereals and coarse grains where procurement takes place at MSP:

- **Price Support Scheme (PSS):** Under this, physical procurement of pulses, oilseeds and copra will be done by Central Nodal Agencies. Besides National Agricultural Cooperative Marketing Federation of India Ltd (NAFED), FCI will also take up procurement of crops under PSS. The expenditure and losses due to procurement would be borne by the Centre.
- **Price Deficiency Payment Scheme (PDPS):** This will cover all oilseeds for which MSP is notified and Centre will pay the difference between the MSP and actual selling/ model price to the farmer directly into his bank account. Farmers who sell their crops in recognized mandis within the notified period can benefit from it.
- **Pilot of Private Procurement and Stockiest Scheme (PPSS):** In the case of oilseeds, the States will have the option to roll out PPSS in select districts where a private player can procure crops at MSP when market prices drop below MSP. The private player will then be compensated through a service charge up to a maximum of 15% of the MSP of the crop.

Significance of the Scheme

- **An innovative MSP-plus approach to the problem of non-remunerative prices:** The three different components of the scheme will **cover gaps in the procurement and compensation** mechanism for crops, thus ensuring remunerative prices for farmers and help reviving rural economy.
- **Ensure crop diversification and reduce stress on soil and water:** Unlike the current system where farmers repeatedly go for the few crops, such as paddy, wheat and sugarcane.
- **Better translation of increased MSP to farmer's income:** by way of robust procurement mechanism in coordination with State Governments.
- **Increased financial provisions:** Centre has made a provision of Rs. 16,550 Crore as a bank guarantee for central agencies to directly procure from farmers under PSS, while budgetary allocations for PM-AASHA has been raised to Rs. 15,053 Crore.
- **It is a significant step towards enhancing productivity,** reducing the cost of cultivation and strengthening post harvesting management, including market structure.

Challenges

- **Agricultural markets must function transparently and government must take steps to break the traders' cartel:** Experience of Madhya Pradesh which implemented the PDPS under **Bhavantar Bhugtaan Yojana** revealed that the traders plotted with each other and depressed the prices at mandis. They forced farmers to sell at lower prices and pocketed the compensation from the government.
- **Providing funds for PSS would be a key challenge for Centre** as State Governments consider it financially burdensome. If all states apply to NAFED/FCI for procurement of oilseeds or pulses, the agencies would fall short of funds.
- **Warehousing and storage infrastructure shortage not addressed:** Many States such as Bihar, Jharkhand, West Bengal and almost entire North-East are unlikely to procure a substantial quantity of paddy at MSP due to weak financial resources and infrastructure constraints of the organizations responsible for paddy procurement.

Way Forward

- **E-NAM and inter-market competition must be promoted:** Centre must break the trader lobbies by widening the competition by inter-linking mandis, and States must proactively undertake regulatory reforms.

- A robust **pro-farmer export policy** must be considered. Simultaneously, **market reforms** including Model Agricultural Produce and Livestock Marketing Act, 2017 and Model Contract Farming and Services Act, 2018 should also be replicated by all the State Governments.
- Successful implementation and effective private participation are the key to overall success of the scheme**.** Guidelines for private participation in consultation with state governments must be formed.

7.3. AGRICULTURAL INSURANCE

7.3.1. PRADHAN MANTRI FASAL BIMA YOJANA (PMFBY)

Why in News?

Out of Rs. 1,400 crore earmarked annually for the north-eastern States under Pradhan Mantri Fasal Bima Yojana, only Rs. 8 crore was actually spent in 2018. Arunachal Pradesh, Nagaland, Manipur and Mizoram are not covered under the scheme at all. This has raised questions on the implementation of the PMFBY.

Features of PMFBY

- It was launched in 2016 replacing the existing two schemes National Agricultural Insurance Scheme (NAIS) as well as Modified NAIS.
- A **uniform premium** of only 2% to be paid by farmers for all Kharif crops and 1.5% for all Rabi crops & oilseeds and 5% for horticultural crops. The balance premium was to be paid by state and central government in equal proportions.
- There is no **upper limit on Government subsidy** so farmers will get claim against full sum insured without any reduction.
- The PMFBY is **compulsory for loanee farmers** availing crop loans for notified crops in notified areas and voluntary for non-loanee farmers.
- The PMFBY operates on an **area approach**. Thus, all farmers in a particular area must pay the same premium and have the same claim payments.
- **Yield Losses** – Natural Fire and Lightning, Storm, Hailstorm, Cyclone, Typhoon, Tempest, Hurricane, Tornado. Risks due to Flood, Inundation and Landslide, Drought, Dry spells, Pests/ Diseases. It also includes Post Harvest losses.
- It also includes **mandatory use of technology** such as smart phones, drones etc. while assessing losses.
- **Public sector insurer** (Agriculture Insurance Company of India, United India Insurance Company etc.) and private insurance companies are empaneled for implementation of the scheme.
- Recently, states have been allowed to set up their own insurance companies for implementing the scheme.
- Recently, Government has comprehensively **revised the Operational Guidelines of the scheme**.
  - The farmers will be **paid 12% interest by insurance companies for the delay in settlement claims** beyond two months of prescribed cut-off date.
  - Inclusion of hailstorms in **post-harvest losses, besides unseasonal and cyclonic rainfalls**.
  - Appointment of District Level Grievance Redressal Officer and creation of State and District Grievance Redressal Cells for **fast redressal of grievances.**

Challenges faced in the implementation of PMFBY

- **Delayed compensation:** Many state governments have failed to pay the subsidy premiums on time, as paying these premiums eat into their budgets for the sector. This leads to insurance companies delaying or not making claim payments.
- **High premium charged:** There was an increase in the premium being charged by the private companies whereas it was expected to be reduced even though they are allotted areas with less risk.
- **Inadequate Data collection:** Data discrepancy, leading to high claim ratios in certain states, has been a major concern, often resulting in delay of settlement. According to insurers, crop cutting experiments (CCE) in the previous years were not properly conducted in several states.
- **Poor capacity to deliver**: Insurance companies are not putting in place any ground infrastructure required for grievance redressal and assessing crop losses in individual plots. Also, there have been no concerted effort by the state government and insurance companies to build awareness of farmers on PMFBY.
- **Declining farmer enrolments**: Between FY16 and FY17, the number of farmers enrolled in the scheme declined from about 57.3 million to about 48.5 million, a fall of around 15 per cent.
- **Issues with notification of crops**: As states have the responsibility to notify crops, there are lack of clarity and wide spread variations in choosing the major crops among the states, which in turn results in the exclusion from insurance coverage of farmers who grow non-notified crops.

Way Forward

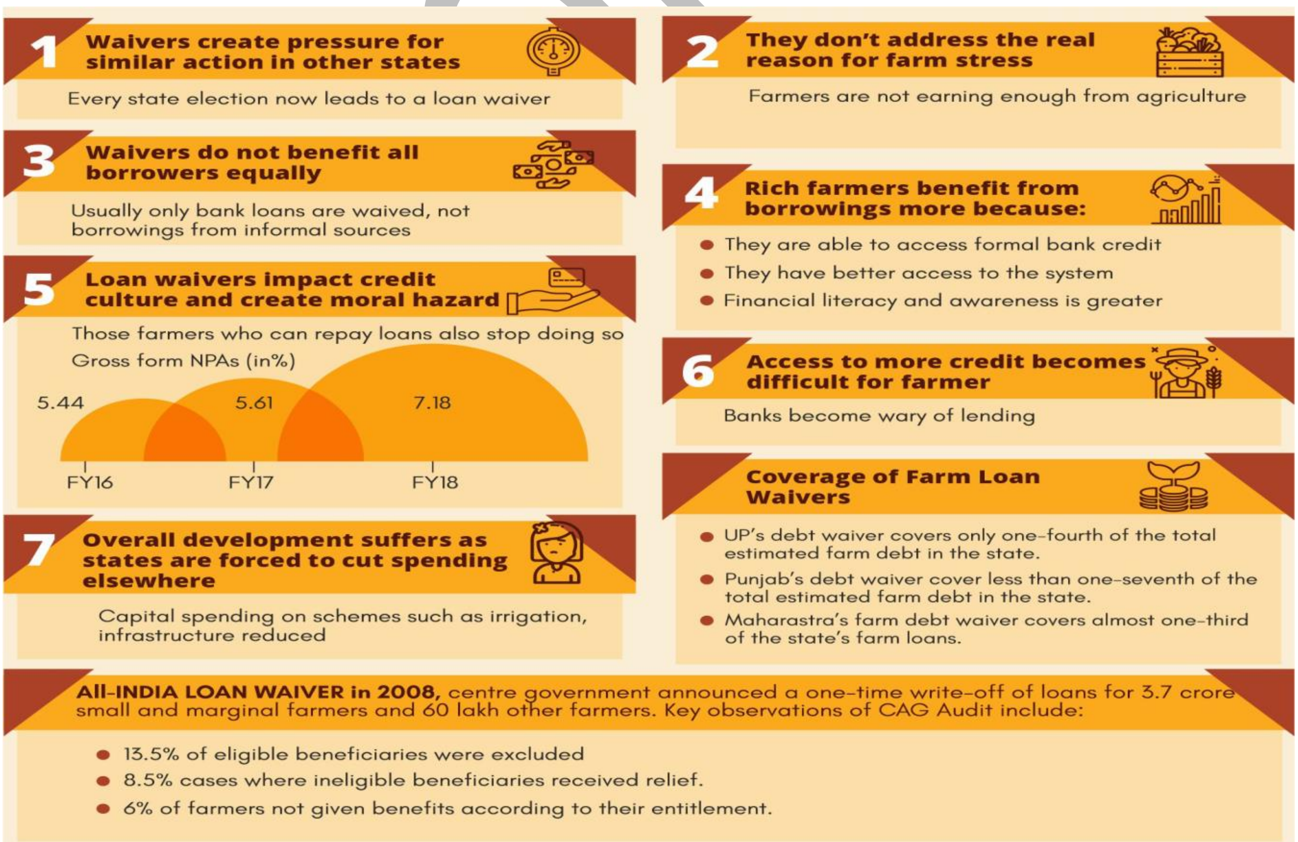
- **Governance**
    - Strengthen the capacity of state governments by increasing funds for rural infrastructure and incentivizing the development and use of technology.
    - It is crucial to increase the penetration of crop insurance. Mandatory awareness programmes on the benefits of crop insurance must be developed.
    - A grievance-redressal system to help distressed farmers resolve issues regarding the scheme.
    - A regulatory framework that unifies the insurance system covering yield and price risk will ensure increased participation and stability.
- **Technology and Infrastructure**
    - The use of remote-sensing, drones, satellite imagery and digitization of land records for effective implementation of the PMFBY.
    - A 360-degree approach where crop insurance scheme should be combined with efforts towards land and water management, including irrigation development, soil conservation and improvement in public delivery systems.
- **Other recommendations**
    - Land lease laws must be changed to achieve larger participation in the welfare programme. The land policy must be dynamic to prevent transformations from stalling, an important concern that needs cooperative federalism to achieve higher productivity in this sector.
    - It is crucial to include women farmers, tenant farmers and sharecroppers to help formalise this economy, protecting revenue and jobs.

7.3.2. FARM LOAN WAIVER

Why in news?

State governments in Madhya Pradesh, Rajasthan and Chhattisgarh, have declared packages for loan write-offs for farmers.

Issues with the Farm Loan Waiver



Macro-economic impacts of Farm Loan Waiver: At its most basic, farm loan waivers simply transfer liabilities from private sector to public sector balance sheets. The waivers will have **four effects on aggregate demand:**

- **Private consumption impact:** Loan waivers will increase the net wealth of farm households pushing consumption up. However, World Bank study in 2008-09 found no rise in consumption after the loan waivers.
- **Public sector impact:** Loan waivers involve spending that does not add to demand (because these are liability transfers to the states' balance sheets) but the actions taken to meet Fiscal Responsibility Legislation (FRL) targets (higher taxes and/or lower expenditure) will reduce demand.
- **Crowding out impact:** Loan waivers will result in higher borrowing by the states with fiscal space. This could squeeze out private spending by firms.
- **Crowding in impact:** Bank balance sheets will improve to the extent that non-performing farm loans are taken off their books. So they might be able to provide additional financial resources to the private sector, leading to greater spending.

Way Forward

The primary reason for persistent farm distress is the inability of farmers to get remunerative prices, due to the prevailing disconnect with the value chain resulting from market asymmetry, and lackadaisical institutional and infrastructure support.

A loan waiver is only an element of immediate relief. **Greater focus is required on enhancing their loan repayment capacity** via smooth supply and value chains, and better price realisations along with farm credit reforms. This could be achieved by following measures:

- **Institutional Strength:** The most important constraint of Indian farmers is their small and uneconomical size of holdings. This can be overcome by
  - Encouraging the formation and working via **farmer producer organisations (FPOs)** that act as aggregators and help farmers overcome their unorganised nature.
  - **Government spending in the creation of suitable storage capacities** - either independently or in public-private partnership (PPP) model- will not only help farmers to store their produce, but also connect them to institutional finance through a much more secure mechanism of warehouse receipt finance through FPOs.
  - Ensure reach of minimum support price & crop insurance across the geography and crops.
- **Better Decision-Making:** Agriculture and markets remain highly disconnected, with poor information flow across unusually long supply chains in most agricultural commodities.
  - An independent national set-up could be created with a PPP at the block/district level to provide necessary information that would empower farmers to make the right decisions- from choice of crop and cropping practices, to harvesting and sales.
    - ✓ This would augment input purchase support to small and marginal farmers, in line with direct cash transfer, as well as strengthen the efficacy of free market mechanism for ensuring remunerative prices.
- **Agriculture Credit Reforms**
  - Extend period of crop loan to four years, to account for the erratic pattern and spatial distribution of rainfall. Like industrial loans, extend provision of restructuring and one-time settlement for industry to farm loans.
  - A specific, region and crop-based scheme of loan concessions and one-time settlement would ensure that credit discipline is not eroded.
  - Institutionalise a mechanism, with a regulatory authority supervising the scheme of de-stressing farm loans, based on a scientific basis for calculating stressed assets and restructuring them. NABARD should be utilised for this purpose.

7.3.3. POLICY BIAS AGAINST RAINFED AGRICULTURE

Why in news?

Recently a **Rainfed Agriculture Atlas** was released, which has pointed out that there are biases against rainfed agriculture in the policies of the government.

About Rainfed Agriculture

- A region is classified as rainfed, if assured irrigation is not provided to majority of the net sown area. It is an interrelation of production systems, natural resources and people's livelihoods in rainfed regions.

- In India they cover around 180 districts and exist in all agro-climatic regions but are mostly concentrated in the arid and semi-arid area. About 61 per cent of India's farmers rely on rain-fed agriculture and 55 per cent of the gross cropped area is under rain-fed farming.

Importance of these areas

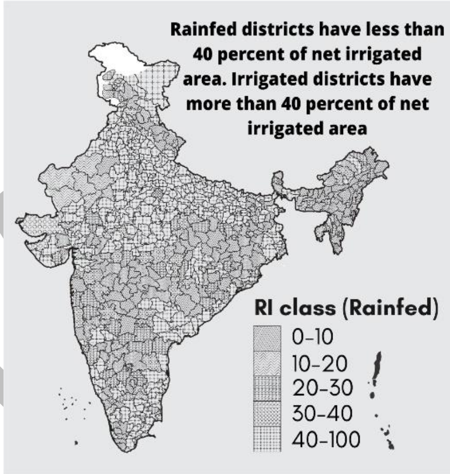
- Rain-fed areas contributed significantly to the country's food production. They account for **88 per cent of pulses and 40 per cent rice production** in the country.
- They also support **64 per cent of cattle population** in the country.

Revitalising Rainfed Agriculture Network

- It was formed in 2010 is a pan India network of more than 600 members, including eminent academics, policy makers, farmer and civil society organisations that work to influence public systems, policy and investments for productive, prosperous and resilient rainfed agriculture.
- It publishes the **Rainfed Agriculture Atlas**.

Inherent issues with Rainfed agriculture

- **Low Incomes of farmers**- While farmers in irrigated areas earn 60 per cent of their income from agriculture, their counterparts in rainfed areas earn only 20-30 per cent from farm-related activities.
- **Majority people in rain fed areas are poor**- There is an overlap of the poorest districts with rainfed districts in various parts of India.
- **Low crop yields** - While the average yield in rain-fed areas is about 1.1 tonnes per hectare, that in irrigated areas is about 2.8 tonnes per hectare.
- **Increasing number of suicides among farmers**- especially in the dry land areas.
- **Ecologically fragile**- One-third of the dry land areas are highly degraded, which cannot be put under cultivation. They receive rainfall of either less than 500 mm or more than 1,500 mm and suffer from serious water management problems either way.
- **Government Policies are not conducive**.



Issues with Current Policies in regard to Rainfed Agriculture

- **Schemes not framed particularly for rainfed agriculture**- Flagship government schemes, such as seed and fertiliser subsidies and soil health cards, are designed for irrigated areas and simply extended to rainfed farmers without taking their needs into consideration.
- **Negative impact on rainfed farms by extension of other schemes**- e.g. Many hybrid seeds notified by the government scheme need plenty of water, fertiliser and pesticides to give high yields and are thus not useful to most rainfed farmers. Commercial fertilisers simply burn out the soil without sufficient water.

Important Government Initiative

National Mission for Sustainable Agriculture (NMSA) – It is envisaged as one of the eight Missions outlined under National Action Plan on Climate Change (NAPCC). The major thrust is enhancing agriculture productivity especially in rainfed areas focusing on integrated farming, soil health management, and synergizing resource conservation.

- **Rainfed Area Development** - It focuses on **Integrated Farming System (IFS)** for enhancing productivity and minimizing risks associated with climatic variability's.
  - Under this system, crops/cropping system is integrated with activities like horticulture, livestock, fishery, agro-forestry, apiculture etc.
  - It enables farmers not only in maximizing farm returns for sustaining livelihood, but also to mitigate the impacts of drought, flood or other extreme weather events with the income opportunity from allied activities during crop damage.

- **Lower Investment on infrastructure**- Lands irrigated through big dams and canal networks get a per hectare investment of Rs. 5 lakh. Watershed management spending in rainfed lands is only Rs. 18,000-25,000 per hectare.
- **Low Procurement from crops in rainfed areas**- From, 2001-02 and 2011-12, the government spent Rs. 5.4 lakh crore on wheat and rice (Irrigated areas). Whereas on coarse cereals, which are grown in rainfed areas, only Rs. 3,200 crore worth of procurement has been done in the same period.
- **Lack of utilization of local expertise**- The government has no system in place to channelise indigenous seeds or subsidised organic manure in the same way.

Way Forward

- **Separate Policy orientation for Rainfed farms**- Need to give rainfed farmers the same research & technology focus, and production support that their counterparts in irrigation areas have received over the last few decades (Green Revolution).
- **Need to enhance productivity of Rainfed areas**- Most of these areas can take up a second crop. Hence, scientific selection of crops **suitable for local agro-climatic zones** should be done.
- **Shift from 'input-centricity' to 'needs/requirements'-centricity**- In the long run, cash incentives and income support like the PM-KISAN scheme announced in the budget earlier this month would be better than extensive procurement.
- **Focus on livestock**- Livestock is an essential component of dryland ecosystems. They provide much needed farmyard manure for maintaining soil fertility apart from being useful for other agricultural operations. The whole livestock support systems are 'milk-centric'. There are practically no support systems available for livestock rearing for most of the farmers of dryland regions.
- Investing in rainfed agriculture would have huge implications for the ecological, social and economic well-being of the large and diverse populations that inhabit it.

7.4. AGRICULTURAL MARKETING

7.4.1. ENDING APMC MONOPOLY

Why in news?

Maharashtra became 2nd state after Bihar to **end the monopoly** of Agricultural Produce Market Committee (APMC) and allow trade in farm commodities including livestock outside the wholesale markets (mandis).

About APMCs

- Presently, the marketing of agricultural commodities is governed by Agricultural Produce Market Committee (APMC) Act enacted by respective State Governments
- The notified agricultural commodities as well as livestock covered under its ambit.
- First sale of crops by farmers - after harvesting - can only take place in APMC authorized mandis (not at the farm gates) through auctions
- To remove discrepancies in agricultural markets, Central Government proposed Model APMC Act, 2003 and **Model Agricultural Produce and Livestock Marketing (Promotion and Facilitation) Act, 2017**.

How the Model APLM Act is different from the Model APMC Act, 2003?

- Intra-state trade made available by paying a single fee.
- Promotion of e-trading in agricultural produce.
- A state may declare any market yard as a Market yard of National Importance (MNI).
- Cap on levy of market fees is proposed at 2% (of sale price) for fruits and vegetables and 1% for food grains.
- All regulatory powers will lie with the office of the director of agricultural marketing in the state, who will also issue licenses to traders and new private players. As of now, this power lies with the mandis - managed by a board of directors.

Why do APMCs need reform?

- **Market Segmentation:** The **monopoly of APMCs** in agriculture market **reduces buyer competition** in comparison to integrated markets, as it limits the geographical range of the mandis, number of buyers and sector specialization of buyers.
- **High Spatial Price Dispersion:** In India, the ratio of the highest price of a commodity to its lowest price - a measure of price dispersion (Economic Survey 2015-16) - is almost thrice that observed in the US. This indicates that markets are not well integrated and logistics cost is high.
- **Cartelization:** Cartelization by traders prevents price discovery mechanisms from functioning in mandis.
- **High Degree of Intermediation:** Farmers' share in consumer prices range from 15% to 40% (Ashok Dalwai Committee). Missing credit markets (farmers borrow from intermediaries, conditional to sale of harvest), lack of storage, high transportation & processing costs add to the retail-farmgate gap. This prevents farmers from realizing higher prices and consumers from buying food at lower prices.
- **High License fees + APMC Cess and Taxes:** High commission levied on both farmers and buyers create artificial inflation. Final price to consumer high but benefit does not reach the farmer.
- **Wastage (poor storage and transportation):** APMCs do no value addition in terms of storage and transport facilities leading to high wastage.

Way Forward

- **Creating Market Infrastructure:**
  - **Physical integration:** Railroad expansion changed the landscape of agricultural markets in US.
  - **Digital integration: e-NAM (National Agricultural Market)** where the entire country must be treated as unified market
- **Changing the target market:** Other states must also modify laws that constrain farmers to sell in local mandis only, especially for perishables. Some complementary measures such as provision of land & financial incentives for private sector-promoted market yards is needed. Farmers can also realize maximum profits by selling the produce directly to food processing units (less rotting & regular supply)
- **Transport and storage infrastructure for perishables:** Transport of perishable commodities in Reefer trucks & freight subsidy would help in better supply and availability of the produce. At present, **India's cold storage capacity** is nearly 3.5 cr tonnes, short by 30-40 lakh tonnes, and it needs to be increased.
- **Establishing Markets of National Importance (MNI):** At present, Asia's largest agricultural market at Azadpur, Delhi is the only Market of National Importance (MNI) in the country. More such markets need to be established to boost inter-state trade.
- **Setting up Farmer Producer Organizations and Cooperatives:** It would provide better avenues at collective bargaining to small & marginal farmers. It could also act as a direct marketing channel to supply produce from 'surplus' regions to high demand states
- **Restructure Essential Commodities Act:** To incentivize corporate companies to invest in trading of agricultural commodities. The exemptions from stockholding limits must be given to exporters, food processors, multiple outlet retailers, large departmental retailers etc.
- **Alternative marketing options:** such as contract farming, direct marketing through FPOs/cooperatives etc, commodity trading through National Commodity and Derivatives Exchange, e-RaKAM (digital spot trading market), NSEL (where warehouse receipts of commodities are traded) etc.
- **Nation-wide Price Dissemination Mechanism:** Forward Market Commission (FMC) has set up **e-portal AGMARKNET** that displays real time wholesale price of agricultural commodities on e-portal connected with APMC markets, Kisan mandis, Kisan Vikas Kendras (KVKs), State Agricultural Boards etc.

Gramin Agricultural Markets (GrAMs)

- The Centre has identified **1,878 rural haats** for modernisation and development of infrastructure through MGNREGA till March 2019 under Gramin Agriculture Markets (GrAM) programme.
- These are owned by Local Bodies (Panchayats/councils), Agricultural/Horticultural Departments of State Governments, Cooperatives, Marketing Boards/APMCs and Private Sector.
- GrAMs to be linked to e-NAM and to be outside the APMC Act regulation.
- **Significance of this move-**
  - It will **ensure participation of small and marginal farmers to markets especially eNAM.**
  - Awareness, coupled with increase in Agricultural & Horticultural production, will **generate larger arrivals in Rural Markets**. Also it will open avenues for non-farm products like livestock etc.
  - It has proposed to **build on the available infrastructure** to establish large number of primary rural agricultural markets to provide the **following two services**: Direct marketing between producers and consumers and aggregation platform for farmers

7.4.2. AGRICULTURE EXPORT POLICY, 2018

Why in news?

- With an **aim to double farmers' income by 2022, and to double agricultural exports by 2022,** Government of India has recently come up with the Agriculture Export Policy, 2018.

Current Agriculture Trade Scenario

- World agricultural trade has been **relatively stagnant in the last five years** (2013-2017) due mainly to fall in global prices.
- Due to effect of fall in global prices and back to back droughts during 2014-15 and 2015-16 **India's agricultural export dropped by 5% compound annual growth rate** (CAGR).
- Indian **agricultural exports grew at 9%** compared to China (8%), Brazil (5.4%) and USA (5.1%) between 2007 and 2016. However, **India's agriculture exports are lower** than countries like Thailand and Indonesia with much smaller agricultural land thus depicting a higher potential.
- While India occupies a leading position in global trade of agricultural products like rice, its **total agricultural export basket accounts for little over 2% of world agriculture trade.**

- Also, India has remained **at the lower end of the global agricultural export value chain** given that majority of its exports are low value, raw or semi-processed and marketed in bulk.
- The **share of India's high value and value added agricultural produce** in its agriculture export basket is less than 15% compared to 25% in US and 49% in China. India is unable to export its vast horticultural produce due to lack of uniformity in quality, standardization and its inability to curtail losses across the value chain.

Objectives of the Agriculture Export Policy

- To **double agricultural exports** from present $ 30+ Billion to $ 60+ Billion by 2022 and reach $ 100 Billion in the next few years thereafter, with a stable trade policy regime.
- To **diversify our export basket**, destinations and boost high value and value added agricultural exports including focus on perishables.
- To **promote** novel, indigenous, organic, ethnic, traditional and non-traditional Agriculture products exports.
- To provide an **institutional mechanism** for pursuing market access, tackling barriers and deal with sanitary and phyto-sanitary issues.
- To strive to **double India's share in world agriculture exports** by integrating with global value chain at the earliest.
- Enable farmers to get **benefit of export opportunities** in overseas market.

Elements of the Agriculture Export Policy Framework

Vision of the Agriculture Export Policy: "Harness export potential of Indian agriculture, through suitable policy instruments, to make India global power in agriculture and raise farmers' income."

The policy recommendations are organized in two broad categories: **strategic and operational**

1. Strategic Recommendations	
Policy Measures	**Stable Trade Policy Regime** • Providing assurance that the processed agricultural products and all kinds of organic products will not be brought under the ambit of any kind of export restriction. • Identification of a few commodities which are essential for food security in consultation with the relevant stakeholders and Ministries. **Reforms in APMC Act and streamlining of mandi fee** • Using the Directorate General of Foreign Trade (DGFT) field offices, Export Promotion Councils, Commodity Boards and Industry Associations to act as advocacy forum for reform by all the states including removal of perishables from their APMC Act. • State govts. would be urged to rationalize mandi taxes for exported agricultural products.
Infrastructure and Logistics Support	• Pre-harvest and post-harvest handling facilities, storage & distribution, processing facilities, roads and world class exit point infrastructure at ports facilitating swift trade. • **Mega Food Parks**, state-of-the-art testing laboratories and **Integrated Cold Chains**. • Identifying **strategically important clusters**, creating **inland transportation** links alongside **dedicated agricultural infrastructure at ports** with 24x7 customs clearance for perishables.
Holistic approach to boost exports	• **Involve important organizations related to agricultural production** to make special efforts towards promotion of export. **Krishi Vigyan Kendras** will be involved to take export oriented technology to farmers and create awareness among farmers about export prospects. • **Work towards similar agencies** like the United States Food and Drug Administration (USFDA) which cover all aspects of agricultural-food production and trade in a effective and calibrated manner. • A holistic response to **Sanitary and PhytoSanitary (SPS)** and **Technical Barriers to Trade (TBT)** barriers faced by Indian products
Greater involvement of State Governments in Agriculture Exports	• Identification of a **nodal State Department / Agency** for promotion of agriculture export • **Inclusion of agricultural exports** in the State Export Policy • **Infrastructure and logistics** to facilitate agricultural exports • **Institutional Mechanism** at Union level, State level and cluster level to support exports • **Encourage the industry bodies/associations** to play a more pro-active role and greater involvement of industry in R&D
2. Operational Recommendations	
Focus on Clusters	• Put in place **institutional mechanism** for effective involvement and engagement of small and medium farmers for entire value chain as group enterprise(s) within **cluster of villages at the block level for select produce(s).** This will help to realize actual benefit and empowerment of farming community to double their income through entire value chain. o Subject to successful implementation of these clusters, a **transition to Agri Export Zones (AEZs)** could facilitate value addition, common facility creation and higher exports from such zones.

	• The **concept of Agri Export Zone (AEZ)** was introduced in 2001, through EXIM Policy 1997-2001, to take a comprehensive look at a particular produce/product located in a contiguous area for the purpose of developing and sourcing the raw materials, their processing/packaging, leading to final exports. • AEZ **focuses on convergence** of existing Central and State Government schemes to take care of financial and policy interventions required at various stages of value chain • In all **60 Agri Export Zones (AEZ)** were notified by the Government till 2004 - 05. **No new AEZs have been set up after 2004.** All the notified AEZs have completed their intended span of 5 years and have been discontinued.
Promoting value added exports	• Product development for **indigenous commodities** and value addition • Promote value added **organic exports** o Marketing and branding of organic products o Develop uniform quality and packaging standards for organic and ethnic products o **Organic products in North East**- development of 'AMUL' – style cooperatives • Promotion of **R&D activities** for new product development for the upcoming markets • **Skill development**
Marketing and promotion of "Brand India"	• Constituting **separate funds** dedicated to marketing of organic, value added, ethnic, GI, Region specific and branded products.
Attract private investments in export oriented activities and infrastructure	• Benefits of private investment include better quality compliance; smooth logistic handling; expansion to distant markets. • The Infrastructure proposed to **support agriculture exports from the Focus States** includes: Packhouse, Processing infrastructure, Exit Point Infrastructure, Air cargo and Infrastructure abroad.
	• **Ease of Doing Business (EODB)& Digitization:** Farm level – digitization of farmer land records, **Market Intelligence cell at Department of Commerce** and Portal for Information dissemination, Trade procedures and facilitation and Grievance cell.
	• **Developing Sea Protocol:** Developing sea protocols **for perishables** must be taken on priority for long distance markets. Export of perishables requires special storage, transportation and handling at desired temperatures where Time is a major constraint.
Establishment of Strong Quality Regimen	• Establish and maintain **single supply chain and standards** for domestic and export market
	• **SPS and TBT Response Mechanism**: it is suggested to **create an institutional mechanism** under the aegis of Department of Commerce with representation of relevant Ministries, Agencies to address India's market access request, calibrate it with trading partner's market access request for accessing the Indian market and quickly respond to SPS/TBT barriers.
	• **Conformity Assessment:** Many importing countries do not recognize India's export inspection and control processes. The lack of recognition of Indian testing procedures and conformity standards proves costly to exporters and therefore farmers.
Research and Development	• Agricultural research and development (R&D) **led by private industry along with higher infrastructure spend by the government** will be the key to boosting agricultural exports. Along with this, innovations in packaging, improving shelf life of products and greater R & D in developing products to suit the palates of importing countries would be a priority.
Miscellaneous	• **Creation of Agri-start-up fund:** Entrepreneurs are to be supported to start a new venture in Agri products exports.

Challenges in Policy Implementation

- Achieving an agriculture export **target of $60 billion by 2022 looks ambitious**, given the current global market conditions. More so, because **India's export basket** largely comprises meat, marine products, and basmati rice whose demand in the world market is inelastic.
- India has a track record to open up imports whenever prices of crucial food items (potato, onion, pulses, etc.) start climbing. This hurts local producers. The **Indian government is always "pro-consumer",** backing cheap imports to keep inflation in food prices low.

> **Related News**
> UAE and Saudi Arabia had decided to **use India as a base to address their food security concerns.** In accordance with the Agriculture Export Policy, the farm-to-port project will be similar to a special economic zone but in the style of a corporatised farm, where crops would be grown keeping a specific market in mind.

- There are several instances of **sudden increase in export duties and lowering of import duties** to keep food prices in check. The Centre cut the import duty on wheat by a fifth when prices increased in 2016-17, leading to imports from Australia and Ukraine flooding the market. Similarly, a zero import duty on palm oil hurts domestic oilseeds farmers.

- The current **minimum support price (MSP)** of wheat and rice make India foodgrain quite dear in the domestic market. In such cases, India cannot export it into the international market.
- A **dispute at the World Trade Organization (WTO)** can also not be ruled out. Already, the United States accuses India of subsidising farmers heavily to keep prices low.

7.4.3. FOOD GRAIN MANAGEMENT IN INDIA

Why in news?

- With food grain stocks held by Food Corporation of India (FCI) in the central pool has hit 6 year high, the Government plans to increase allocations to below-poverty-line (BPL) families.
- Additionally, the Food Corporation of India has commissioned a new roadmap to speed up silo construction to meet its target of 100 lakh tonnes of storage space by 2022.

About FCI

FCI was set up in 1965 (under the Food Corporation Act, 1964) with three basic objectives:

- provide effective price support to farmers by procuring the crop at Minimum Support Price (MSP) if they are not able to sell it in Agricultural Produce Marketing Committee (APMC) authorized mandis
- procure & supply grains to PDS for distributing subsidized staples to economically vulnerable sections of society
- keep strategic reserve to stabilize markets for basic food grains.

About Food grain Management in India

- **Food Corporation of India (FCI)** is the nodal agency under **Ministry of Consumer Affairs, Food and Public Distribution** responsible for the procurement, storage and movement of food grains, public distribution and maintenance of buffer stocks.
- FCI **procures food grains** at minimum support price (MSP) from farmers on an **open-ended basis** (i.e., accepting all the grains that are sold to it by farmers), provided the food grains meet Govt. of India's uniform quality specifications. The procurement is also done by State Government Agencies (SGAs) and private rice millers on behalf of the FCI.

Why there is a problem of excess buffer stocks?

- **Oversupply of food grains** due to skewed cropping pattern. **Excess production** of food grains due to higher MSPs, additional bonuses offered on food crops by the states and no viable export outlets.
- **Lack of coordination** between FCI and Consumer Ministry which decides buffer norms.
- **Open ended procurement** i.e. procures all food grains supplied to it by farmers, state agencies etc.
- **No automatic liquidation rule:** Ideally, FCI should sell all grains above buffer stocks in open markets. But, there is no such rule and offtake happens only on the directive of the ministry.

- All the procured food grains form the Central Pool. The grains are moved from the surplus states to the **consuming states for distribution** and **for creation of buffer stocks** and stored in FCI godowns.
- The food grains are also disposed by FCI and State Governments through sale under **Open Market Sales Scheme (OMSS)** i.e., selling food grains at predetermined prices in the open market from time to time to enhance the supply of grains especially during the lean season and thereby to moderate the open market prices especially in the deficit regions.
- The **economic cost to FCI** includes **acquisition cost of food grains at MSP**, **procurement incidentals** (e.g. labour & transport charges, godown rentals) and **distribution cost** (freight, handling, storage & interest charges, losses during storage etc).
  - **Difference between Economic Cost and Central Issue Price (CIP)** of food grains under various schemes (including National Food Security Act, 2013) is the operational loss to FCI and is **reimbursed by Government of India as food subsidy**.

Issues with India's food management system

- **Excess of buffer stocks:** Open ended grain procurement has increased food grain stockpiles beyond the needs of food security. E.g. By June 2019, FCI and state agencies stockpiled 76.1 million tonnes of staples (wheat and rice) against the requirement of 61 million tonnes.
- **Lack of storage:** Due to inadequate number of godowns for storage, a part of procured grains is maintained as outdoor stacks ('Cover-and-Plinth' system), which face high risk of rain damage and pilferage.
- **Food inflation:** More than 75% of the marketable surplus is procured by the Government. Such stocking of food grains which otherwise could have been sold in open markets adds to food inflation.

- **Poor quality of food grains & high wastage:** Due to insect infestation, microbiological contamination, physiological changes due to sprouting and ripening etc., the shelf life of food grains remain poor. Lack of irradiation facilities also impedes long term storage.
- **High costs for government:** Fiscal load of procuring, carrying & maintaining excess stock is over ₹1 trillion and adds to the food subsidy bill.
- **Countercyclical procurement policy:** In drought years, when the production is low, Government increases MSP and stock uptake from farmers. This reduces the supply of grains in open market and pushes the prices high.
- **Marginalization of private trade:** Existing system of food grain management in India is **dominated by the Government**, right from production (as cropping pattern is influenced by MSPs) to stocking (FCI) and marketing (APMCs).
    - Even in traditionally high producing states like Punjab and Haryana, private trade been marginalized due to **open ended procurement** by FCI.
    - Further, **limitations on private stock holding** and **additional state levies** make private participation unviable.
- **Uncompetitive Exports:** Additional state levies make Indian exports uncompetitive in global markets. Moreover, reactionary policies like rising **minimum export price (MEP)** and putting **ceiling limits on exports to check food inflation** adversely affected India's exports in food grains.
- **Corruption:** According to Shanta Kumar Committee, **40-60% PDS food grains** are siphoned from FCI godowns to **black markets**. Many such scams, like Punjab Wheat Procurement Crisis 2016, have come into the light recently.
- **Economic Burden on FCI:** FCI incurs the cost of around Rs. 23 per kg for wheat, which then gets sold at Rs. 2/kg under the National Food Security Act. However, Ministry of Finance constantly underpays FCI to keep in check food subsidy numbers and as a result, it has to borrow money commercially leading to an extra interest burden (Rs. 35,700 cr between 2011-16).

Way Forward

- There is a need to **reorient crop production in favour of high value & export worthy products** E.g. Paddy can be substituted in north-western non-rice consuming region of India with basmati, cotton, maize, soyabean etc which are in high demand domestically and abroad. Haryana has started incentivising farmers to sow alternative crops.
- Procurement as a means of price support can be **replaced with price deficiency payment and direct income support** to the farmers, as envisaged in PM-AASHA and PM-KISAN schemes.
- **Excess buffer stocks can be allocated to poor over and above their monthly quota** of 5 kg under National Food Security Act (NFSA).
- Further, decentralization in procurement should be encouraged. **Decentralized Procurement Scheme (DCP)**, introduced to reduce transport cost and leakages, has been adopted by a very few states.
    - Under this scheme, the respective state governments themselves will procure food grains from farmers on the behalf of FCI and distribute them among poor beneficiaries.
- Lastly, FCI needs an organizational overhaul to make it more functionally efficient. Efficiency is even more important consideration to prevent 'moral hazard' as it is bound to operate under operational losses.

Restructuring FCI

To address the aforementioned issues in food management in India and restructure the role of Food Corporation of India, a High Level Committee was setup under **Shanta Kumar** in 2014. Its important recommendations include-

- **Procurement:** Downsize FCI by outsourcing many of its tasks to state govt., public sector bodies & private companies.
    - Grain procurement, especially in production surplus states like Punjab, Haryana etc, should be delegated to State governments.
    - FCI should focus more on its price support operations in Eastern states like UP, Bihar, West Bengal, Assam etc. where majority of the farmers are small and marginal.
    - FCI should not procure more grains (beyond the quantity needed for PDS) from states offering additional bonuses.
    - On FCI procurements, State government levy commission between 2% to 15%. Uniform rate (~3-4%) should be fixed for entire India.
- **Procurement Payment Systems:**
    - Popularize **Negotiable Warehouse Receipts (NWRs)** system. Under this system, farmers can deposit their produce to the FCI authorized warehouses, and can get advance from banks against their produce valued at

MSP. This will bring back the private sector, reduce massively the costs of storage to the government, and be more compatible with a market economy.
  - No need of physical procurement if market prices are less than the MSP. Farmers should be given the difference the two, through DBT directly into their bank accounts.
- **Buffer stocks:** Only a stripped-down buffer stock of 10 million tonnes should be maintained and grains should be imported in case of dire need. The government can also buy **options/futures in commodity markets** to hedge future price risks.
- **Storage Reforms:**
  - Outsource grain-storage function to central warehousing corporation (CWC), state warehousing corporation (SWC), and private sector players.
    - ✓ **Private Entrepreneur Guarantee (PEG) Scheme** to construct godowns in PPP mode
    - ✓ **Grameen Bhandaran Yojana** to provide capital investment subsidy scheme to build and renovate rural godowns
  - Replace **"cover and plinth" godowns with "Silos"** with mechanized / robotic assemblies
- **Transport Reforms:**
  - Transport grains **in containers rather than gunny bags** to reduce losses and faster-turn-around time at railways and waterways.
  - Construct **silos at mandis**, and provide **rail connectivity** to them
  - **Perishable commodities** should be **transported in Reefer Vehicles** for refrigerated transport
  - **End to End computerization and online tracking** from procurement to retail distribution
- **MSP Policy:** Revisit highly skewed incentive structure in favour of wheat and rice and provide better price support operations for pulses and oilseeds.
- **Pro Active Liquidation Policy for Excess Buffer Stocks:** Whenever FCI's inventories have grains above buffer norms, it should automatically **sell excess stock in open market (domestic or exports).**

7.5. ALLIED SECTORS

- Agriculture and Allied sector plays a vital and critical role in the process of economic development of India by reducing poverty, unemployment & inequality, income diversification, ensuring food security and achieving sustainable development.
- In recent years, Indian agriculture and rural areas are undergoing a considerable change. Rural India is becoming less and less agricultural, and allied activities are becoming an important part of livelihood strategies.
- Shifts in the consumption pattern with rising incomes reflects increase in demand for these products as incomes rise and poverty declines in India. Besides, there exist vast export markets for many of these products which offer an important avenue to enhancing productivity, wages and incomes.
- **Steps being taken for promotion of allied activities**
  - **Integrated Farming system**, which focuses on horticulture, livestock, and bee keeping along with agriculture. This scheme will not only increase farmers' income, it will also mitigate the effect of drought, flood, and other natural disasters.
  - **Rashtriya Krishi Vikas Yojana- Remunerative Approaches for Agriculture and Allied sector Rejuvenation (RKVY-RAFTAAR):** To make farming a remunerative economic activity through strengthening the farmer's effort, mitigating risk and promoting agribusiness entrepreneurship.
  - **National Agro-Forestry Policy**: It has been prepared for increasing the income of farmers and for achieving climate support. During the year 2016-17, a special scheme "Agriculture Forestry Sub-mission" was started and operated with the aim of "Har Medh Par Pedh".
  - **Reconstituted National Bamboo Mission:** Under it Bamboo cultivation is promoted to diversify farmers Income. **The Indian Forest Act, 1927** was amended, to remove bamboo rom the definition of 'trees' so as to promote its hassle free production and marketing.
  - **White Revolution** through conserving indigenous breeds under Rashtriya Gokul Mission, improving genetic makeup, increasing milk production, establishing Dairy Processing and Infrastructure Development Fund, generating self-employment opportunities through Dairy Entrepreneurship Development Scheme
  - **Beekeeping**: is promoted through training large number of farmers/beekeepers, registering bee keepers and honey societies/companies/firms, establishing Integrated Bee Keeping Development Centres (IBDC).

7.5.1. FISHERIES

Why in news?

The Cabinet Committee on Economic Affairs chaired by the Prime Minister has given its approval for creation of special **Fisheries and Aquaculture Infrastructure Development Fund (FIDF).**

Fisheries and Aquaculture Infrastructure Development Fund (FIDF)

Features of FIDF

- **Funding:** The approval entails an **estimated fund size** of Rs.7,522 crore, comprising Rs.5,266.40 crore to be raised by the Nodal Loaning Entities (NLEs), Rs. 1,316.6 crore beneficiaries contribution and Rs.939.48 crore budgetary support from the Government of India.
- **Nodal Loaning Entities:** National Bank for Agriculture and Rural Development (NABARD), National Cooperatives Development Corporation (NCDC) and all scheduled Banks shall be the Nodal Loaning Entities.
- **Financing investment activities:** FIDF would provide concessional finance to State Governments/UTs and State entities, cooperatives, individuals and entrepreneurs etc., for taking up of the identified investment activities of fisheries development.

Benefits of FIDF

- **Rise in production:** To augment fish production to achieve its target of 15 million tonne (MT) by 2020 set under **the Blue Revolution**; and to achieve a sustainable growth of 8% -9% thereafter to reach the fish production to the level of about 20 MT by 2022-23.
- **Employment opportunities:** It will give employment to over 9.40 lakh fishers/fishermen/fisher folk and other entrepreneurs in fishing and allied activities.
- **Rise in Investment:** The credit facilities will help attract investment in creation and management of fisheries infrastructure facilities.
- **Innovation:** Facilitate adoption of **new technologies** such as Open sea cage farming

Fisheries Sector in India

- India has **vast potential** for fisheries considering long coastline of about 8118 km, and an Exclusive Economic Zone (EEZ) of 2.02 million sq Km apart from the inland water resources.
- **Fish production** in India is estimated at 11.4 million tonnes, out of which 68% is registered from inland fisheries sector and the remaining 32% from marine sector.
- India is the **second largest producer** of fish and fresh water fish in the world.
- Constituting about 6.3% of the global fish production, the sector **contributes to 1.1% of the GDP and 5.15% of the agricultural GDP.**
- The fisheries sector is a source of **livelihood for over 14.49 million people**. Besides, an equal number are engaged in ancillary activities in fisheries and aquaculture.
- **Blue Revolution:** Integrated Development and Management of Fisheries approved by the Government provides for a focused development and management of the fisheries sector to increase both fish production and fish productivity from aquaculture and fisheries resources of the inland and marine fisheries sector including deep sea fishing.

Government Steps taken towards fisheries sector-

For Inland Fishing

- Launched Centrally Sponsored Scheme on "**Development of Inland Fisheries and Aquaculture**" under macro-management approach in various states.
- Government had constituted a committee under Dr. Dilip Kumar to draft a national policy on inland fishing.

Draft National Inland Fisheries and Aquaculture Policy (NIFAP), 2019

- **Inland fisheries:** The policy measures recommended:
  - conserving indigenous resources, and restoring natural ecosystem of rivers, wetlands etc.
  - transferring management of fisheries in manmade reservoirs to the state fisheries departments.
  - development of fisheries in the Himalayan and north-eastern states.
- **Aquaculture:** Measures recommended:
  - developing state and area-specific action plans,
  - redefining land use categories to include fisheries and aquaculture as components of agriculture,
  - encouraging private sector in production of seed, feed and other aquaculture inputs.

For marine fishing

- Government had notified **National Policy on Marine Fishing** 2017, "Letter of Permit"(LOP) system in the exclusive economic zone (EEZ) has been stopped in order to boost the livelihood of local fisherman.
- Traditional fishers have been exempted from the fishing ban implemented during monsoon period in the EEZ.

- Prohibited the use of LED lights and other artificial lights and practice of bull-trawling, purse seining and gill netting operations in the Indian EEZ to protect the marine ecology.
- Government has prepared a Census of fishermen, preparing a database of fishing activities, installing tracking devices in fishing boats operating in the waters in averse the accident on boast/vessel.

Draft Policy on Mariculture

- A **draft national policy on Mariculture** has been formulated to ensure **sustainable farmed seafood production** for the benefit of food and nutritional security of the nation.
- Mariculture is a specialised branch of aquaculture involving the **cultivation of economically important marine plants and animals** in the sea or any other water body having **tidal influence** and includes onshore facilities like hatcheries, nursery rearing and grow out systems using seawater. It is generally practiced in the sea up to 12 nm from the coast and also in water bodies which have a salinity regime close to seawater.
- Globally, aquaculture has emerged as the **fastest growing food production sector** with an annual growth rate of >6% in the last two decades. Mariculture is the **fastest growing subsector** of aquaculture and has very high growth potential.
- **Key Provisions of the Policy-**
    - **Mariculture Area Development.**
    - **Farming exotic mariculture Systems and Species**
    - **Addressing seed and feed scarcity**

    Provide **additional livelihood options**

Way Forward

- **On par with agriculture:** Aquaculture needs to be treated at par with agriculture in terms of water, power tariff, tax benefits, subsidy, insurance and credit.
- **Implementation of Dr.B Meenakumari committee** recommendations such as creation of buffer zone (between 200 metres and 500 metres in depth) and scientific use of fishing net should be implemented.
- **Special insurance system** for the fishing community and cooperation in safety and security of fishermen with neighbouring countries should be paramount to averse the loss of many fishers lives.
- **Revival of cooperative sector** with constant engagement of center government would help in achieving the doubling the famers Income 2022.
- **Diversification of sources**: other resources such as upland water bodies, floodplain lakes and wetlands, irrigation canals, saline and waterlogged areas also need to be gradually mainstreamed to start contributing to the production.
- **Productivity augmentation**: Programmes aimed at production and distribution of quality seed and feed for aquaculture and also culture-based-capture fisheries, husbandry of farmed species would be essential to optimize production and productivity.

7.5.2. HORTICULTURE

Why in News?

Ministry of Food Processing Industries (MoFPI) has approved the operationalisation strategy for **Operation Greens (Central Sector Scheme).**

Details

- Operation Greens was announced in the Budget speech of 2018-19 with an outlay of Rs 500 crores **to stabilize the supply of Tomato, Onion and Potato (TOP) crops** and to ensure availability of TOP crops throughout the country round the year without price volatility.
- The Centre has identified **17 top producing clusters across 8 states** (Maharashtra, Bihar, Gujarat, Andhra Pradesh, Uttar Pradesh, Karnataka, Odisha and West Bengal) for the first phases of this initiative.
- The government also intends to utilize the 28 centres of excellence **under Indo-Israel Cooperation** for the demonstration of new technologies in production and the supply of quality planting material and capacity building to farmers under the scheme.
- Government has laid down special **strategy and grants-in-aid** under the scheme to ensure enhanced production of TOP crops and to augment value chain.

Horticulture in India- Related facts

- Over the last decade, the area under horticulture grew by 2.6% per annum and annual production increased by 4.8%.
- India witnessed the shift in area from food grain towards horticulture crops over last five years (from 2012-13 to 2017-18).
- India is second largest producer of Vegetables and Fruits.
- The total horticulture production was highest in case of Uttar Pradesh (392.48 Lakh Tonnes) followed by West Bengal (324.2 Lakh Tonnes).

Major objectives of "Operation Greens"

- Enhancing value realisation of TOP farmers by targeted interventions to **strengthen TOP production clusters** and their Farmer Producers Organizations (FPOs), and linking/connecting them with the market.
- **Price stabilisation** for producers and consumers by proper production planning in the TOP clusters and introduction of dual use varieties.
- **Reduction in post-harvest losses** by creation of farm gate infrastructure, development of suitable agro-logistics, creation of appropriate storage capacity linking consumption centres to increase shell life.
- **Increase in food processing capacities** and value addition in TOP value chain with firm linkages with production clusters.
- **Setting up of a market intelligence network** to collect and collate real time data on demand and supply and price of TOP crops.

7.6. AGRICULTURAL EDUCATION

Why in News?

ICAR has recently launched Rs 1100 crore ambitious **National Agricultural Higher Education Project** (NAHEP) to **attract talent and strengthen higher agricultural education** in the country.

Need of Agricultural Education

- **Increases Agricultural Productivity**: Effective agricultural education (both for farmers as well as researchers) leads to better economic and technical decision making in agricultural processes, which is further reflected in increase in agricultural productivity.
- **Understanding Value Chain of Agriculture:** The entire value chain of agriculture i.e. from farm input to market linkages, suffers from various bottlenecks which can well be addressed by agricultural education.
- **Creates Employment:** Agricultural education is needed in order to absorb the emerging labour force, especially with the emerging arenas of biotechnology, GM food, precision agriculture etc. which require detailed knowledge.
- **Increases Labour value:** Market value of individual in agricultural field in India is lower than many developing countries and agricultural education adds to an individual's productivity and therefore increases the market value of his labour.

Challenges face by Agricultural Education

- **Inadequate Finance:** Agriculture is a state subject and the statutory responsibility for it vests with the state governments which lack in funds. Moreover, the establishment cost of agricultural universities has risen substantially while the operational budget has reduced which constrains institution for innovation.
- **Faculty:** State Agricultural Universities (SAUs) are facing non-replacement of retired faculty and high inbreeding of faculty (nearly 51% of faculty members have their degrees from the same university in which they are teaching), which hampers the quality of academic and research programmes.
- **Lack of Networking and quality:** It has been noticed that most of the universities are lacking in association and integration with different national and international universities for academic activities.
- **Low quality**: The quality provided in these universities is low which further affects their global ranking.
- **Not a first option**: Negative attitude towards agricultural education due to low returns and limited career opportunities makes agricultural education not a preferred choice amongst students.

About NAHEP

- **Funding:** It will be funded by the World Bank and the Indian Government on a 50:50 basis.
- **Objective:** To support Participating Agricultural Universities (AUs) and ICAR in providing more relevant and higher quality education to Agricultural University students.
- **Advantage:** It addresses quality by supporting interested AUs to propose and implement technically sound and verifiable investments that increase faculty performance, attract better students to these AUs, improve student-learning outcomes and raise their prospects for future employability, particularly in the private sector.

Components

- **Institutional Development Plans (IDPs):** NAHEP would provide **Institutional Development Grants** to selected participating AUs, which seek to improve learning outcomes and future employment for AU students and faculty teaching performance and research effectiveness.
- **Centre of Advanced Agricultural science & Technology (CAAST):** CAAST Grants will be provided to selected participating AUs to establish multidisciplinary centers for teaching, research and extension on critical and emerging agricultural topics.
- **Innovation Grants to selected participating AUs** to make AUs reform ready (i.e., attain accreditation); and promote mentoring of non-accredited AUs by existing reform-ready AUs and other interstate and international academic partnerships.
- **Results Monitoring and Evaluation:** The Education Division/ ICAR would establish a **Monitoring and Evaluation (M&E) Cell** to oversee the progress of activities across all NAHEP components.

8. INDUSTRIAL POLICY AND ASSOCIATED ISSUES

Introduction

- Despite being one the fastest growing economies, the striking aspect of India's recent growth has been the dynamism of the service sector. While, manufacturing has been much less robust, contrary to the experience in other emerging market countries, where manufacturing has grown much faster than GDP.
- The gap in both, the sectoral share of manufacturing and the competitiveness of the manufacturing sector in India, compared with other big economies has been increasing which is a matter of concern.
- The industrial sector performance during 2018-19 has **improved** as compared to 2017-18. The growth of industry real Gross Value Added (GVA) was higher at 6.9 per cent in 2018-19 as compared to 5.9 per cent in 2017- 18.

Constraints to Industrial Growth

- **Inadequate infrastructure**: Physical infrastructure in India suffers from substantial deficit in terms of capacities as well as efficiencies.
- **Restrictive labour laws:** It discourages employers from hiring workers on a regular basis. It has probably also led to entrepreneurs choosing to stay away from labour intensive sectors.
- **Complicated business environment:** which adversely affects competitiveness of manufacturing.
- **Slow technology adoption:** this has led to low productivity and higher costs adding to the disadvantage of Indian products in international markets.
- **Low productivity:** Productivity as measured by value added per worker and average wages in manufacturing in India are only one-third of that in China.
- **Challenges for trade:** challenges of stagnant/shrinking global demand, tough competition from cheap imports (China) and rising protectionist tendencies around the world.
- **Inadequate expenditure on R&D and Innovation**

Opportunities for the Indian Industry in the current economic scenario

- India continues to be **a low-cost economy**.
- India has a **relatively higher proportion of a youth** population.
- India is **continuously rated as a top investment destination**. FDI inflow helps to not only meet the gap in domestic savings but also facilitate benefits in terms of the managerial and technological skill.
- India continues to have **a dominating position in the IT sector.** Its dominance at present is in software services. It can avail the opportunity of having dominance in hardware as well.
- A tax reform, GST will turn India into one common market for producers and consumers.
    - It will also probably bring an end to the practice of cherry-picking by the industries which was enjoyed by them on account of area-based exemptions offered by the State Governments and build up a uniform business environment across the country.

It is also to be understood that these factors work in tandem to increase costs of goods and services. They are strongly entwined, one feeds into another thereby exacerbating the disadvantages. The nexus needs to be broken at more than one link to ensure that the spin-off is in the positive direction.

Recommendations of the Parliamentary Standing Committee on Commerce report on 'Industrial Policy in the Changing Global Scenario'-

- **Research and Development**: The R&D in industrial sector needs to be institutionalised and greater connect with universities/IITs needs to be explored by industries
- **IPR Framework**- It must ensure that no higher IP standards of protection may be agreed to other than those included in TRIPS.
- **National Manufacturing Policy**
    - It should be reoriented to **promote smart manufacturing** whereby zero emission, zero incident, zero-defect manufacturing becomes the order of the day.
    - Revisit **Technology Acquisition and Development Fund (TADF)** framework to facilitate smooth induction of smarter industrial processes and sustainable practices in our manufacturing sector to make it smart and ready to enter the **Fourth Industrial Revolution**.
    - **Revive the investments** in **capital goods industries**.
- **MSME Sector** - Access to information, simplification of loan procedures and interest subvention should be enabled for timely and affordable credit to MSMEs
- **Labour and Industrial growth**- Reduction and simplification of the plethora of laws existing in the labour sector.

- **Greater skill-industry interface**- The focus of **vocational training** offered in India is badly mismatched with the needs of workers, so proper alignment of skill development programme to the needs of the workforce is necessary

8.1. MICRO, SMALL AND MEDIUM ENTERPRISES

Why in news?

Recently, the report of the **'Expert Committee on Micro, Small and Medium Enterprises'** under the chairmanship of **U.K. Sinha** was released by the Reserve Bank of India.

Definition of MSME		
Classification	**Manufacturing Enterprise (Investment in Plant and Machinery)**	**Service Entreprise (Investment in Equipment)**
Micro	Upto Rs. 25 lakh	Upto Rs. 10 lakh
Small	Above Rs. 25 lakh to 5 crore	Above Rs. 10 lakh to 2 crore
Medium	Above Rs. 5 crore to 10 crore	Above Rs. 2 crore to 5 crore

Key challenges being faced by MSMEs

- **Limited capital**: Absence of adequate and timely **banking finance**, as per Economic Survey 2017-18, the MSME received **only 17.4 per cent of the total credit** outstanding as of November 2017.
- Problem of **delayed payments** is faced by MSMEs due to various reasons, which increase the financial crunch for their businesses.
- Due to their lack of scale and in-house capabilities, MSEs find it **difficult to access proper market** for selling their products.
- Large-scale presence of MSMEs in **informal sector**, which doesn't allow them to use different assistance available to MSMEs.
- Non-availability of **suitable technology**, creating public perception of products with low quality standards.
- **Low production** due to reasons such as Ineffective marketing strategy, constraints on modernisation & expansions etc.
- **Deficiencies in basic infrastructural facilities** like water, power supply, road/rail and telephone connectivity, etc.
- There are large numbers of clusters but the **resource availability** for undertaking cluster development activities is limited.
- A huge divergence persists between **research institutions** (suppliers of technology) and the business **requirements of MSMEs** (consumers of technology)
- Presently, MSMEs must do **multiple registrations** with various entities such as Udyog Aadhaar portal, GSTN, NSIC, etc. This leads to cumbersome registration process and duplication of efforts.

Importance of MSME sector in India:

MSMEs contribute around 6.11% of the manufacturing GDP and 24.63% of the GDP from service activities as well as 33.4% of India's manufacturing output and around 40 per cent to total exports.

Key Results of NSS 73rd Round Survey (2015-16) on Micro, Small and Medium Enterprises

- The sector comprises of 633.88 lakh units (51.25% MSMEs were in rural area and 48.75% were in the urban areas). The Micro sector accounts for more than 99% of total estimated number of MSMEs. Small sector and Medium sector accounts for 0.52% and 0.01% of total estimated MSMEs, respectively.
- Uttar Pradesh had the largest number of estimated MSMEs with a share of 14.20% of MSMEs in the country followed by West Bengal with a share of 14% again. The top 10 States together accounted for a share of 74.05% of the total estimated number of MSMEs in the country.
- 31% MSMEs were found to be engaged in Manufacturing activities, while 36% were in Trade and 33% in Other Services.
- Male owned 79.63% of enterprises as compared to 20.37% owned by female.
- The socially backward groups owned almost 66.27% of MSMEs, though bulk of that can be attributed to OBCs owning in 49.72%. The representation of SC and ST owners in MSME sector was low at 12.45% and 4.10% respectively.
- It has created 11.10 crore jobs out of which 76% are male employees and remaining 24% are females.

Recent Steps by the Government to help MSMEs

- **MSME Outreach Programme**, which ran for 100 days covering 100 Districts throughout the country. Various Central Ministers visited these districts in order to apprise the entrepreneurs about various facilities being extended to MSME Sector by the Government and financial institutions.
- Reserve Bank of India (RBI) has asked the banks to link the **floating interest rate on retail loans and loans extended to micro and small businesses** to external benchmarks like Repo Rate or Treasury Bills.

Government Support to MSMEs-

Credit and Financial Assistances to MSMEs

- **59-minute loan portal to enable easy access to credit for MSMEs:** A link to this portal will be made available through the GST portal.
- **Interest Subvention:** A 2 percent interest subvention will be provided for all GST registered MSMEs, on fresh or incremental loans. For exporters who receive loans in the pre-shipment and post-shipment period, there will be an increase in interest rebate from 3 percent to 5 percent.
- **Cash flow certainty:** All companies with a turnover more than Rs. 500 crore, must now compulsorily be brought on **the Trade Receivables e-Discounting System** (TReDS). Joining this portal will enable entrepreneurs to access credit from banks, based on their upcoming receivables. This will resolve their problems of cash cycle.
- **Prime Minister's Employment Generation Programme (PMEGP)** is aimed at generating self-employment opportunities through establishment of micro-enterprises in the non-farm sector by helping traditional artisans and unemployed youth.
- **Credit Guarantee Scheme for Micro and Small Enterprises** covers collateral free credit facility (term loan and/or working capital) extended by eligible lending institutions including Non-Banking Financial Company (NBFC) to new and existing micro and small enterprises up to 2 crore per borrowing unit.
- **Credit Linked Capital Subsidy Scheme (CLCSS)** aims at facilitating technology upgradation of the MSME sector.
- The Government has also initiated the **Pradhan Mantri Mudra Yojana** for development and refinancing activities relating to micro industrial units.

Skill Development and Training

- **A Scheme for Promotion of Innovation, Rural Industry & Entrepreneurship (ASPIRE)** to create a framework for start-up promotion through Network of Technology Centres and Incubation and commercialisation of Business Idea Programme.

Infrastructure

- Scheme of Fund for Regeneration of Traditional Industries (SFURTI)
- Scheme for Micro & Small Enterprises Cluster Development Programme (MSE-CDP)

Marketing Assistance

- Scheme for providing financial assistance to Khadi institutions under **MPDA (Market Promotion Development Assistance).**
- MSME Delayed Payment Portal – **MSME Samadhaan**
- Public Procurement Portal for MSEs – **MSME Sambandh**
- **Mandatory public procurement:** Public sector companies have been mandated to compulsorily procure 25 percent, instead of 20 percent of their total purchases, from MSMEs.
- **Women entrepreneurs:** Out of the 25 percent procurement mandated from MSMEs, 3 percent now be reserved for women entrepreneurs.
- **GeM Portal:** All public sector undertakings of the Union Government must now compulsorily be a part of GeM. They should also get all their vendors registered on GeM.

Technology Upgradation and Competiveness

- **Financial Support to MSMEs in ZED (Zero Defect and Zero Effect) certification** to encourage MSMEs to upgrade their quality standards in products and processes with adoption of Zero Defect production processes and without impacting the environment, etc.

Ease of Doing Business

- **Support to pharma companies:** Clusters will be formed of pharma MSMEs and 70 percent cost of establishing these clusters will be borne by the Union Government.
- **One annual return:** The return under 8 labour laws & 10 Union regulations now to be filed only once a year.
- **No more inspector raj:** Now the establishments to be visited by an Inspector will be decided through a computerised random allotment and inspectors must upload reports on portal within 48 hours.
- **Relaxation in environmental clearances:** As part of establishing a unit, an entrepreneur needs two clearances namely, environmental clearance and consent to establish. Under air pollution and water pollution laws, now both these have been merged as a single consent. Moreover, the return will be accepted through self-certification.

Other services

- **National Scheduled Caste and Scheduled Tribe Hub** to provide professional support to SC/ST entrepreneurs.

Key Recommendations of the Committee

- **Review of the legislative framework-** The Micro, Small & Medium Enterprises Development (MSMED) Act, 2006 may be reimagined as a comprehensive and holistic MSME Code having a provision for sunset on plethora of complex laws scattered all over the legislative framework.
- **Change in the definition of MSMEs-** from current investment based to **turnover-based definition,** as it would be more transparent, progressive, easier to implement. It will also remove the bias towards manufacturing enterprises in the existing definition.

- **Strengthening the procurement mechanism-** by promotion of the Government e-Market (GEM) Portal and improving its payment system.
- **Role of different agencies-**
  - o **State Financial Corporations (SFC)-** are setup to promote Small Scale Industries and they can be given more operational freedom by the State legislations.
  - o **Khadi and Village Industries Commission (KVIC)-** should be corporatized with focus on promotional work.
- **Exit Policy for MSMEs-** Due to the lack of sophistication on the part of MSMEs, **Insolvency code/ delegated legislation** should provide for out-of-court assistance to MSMEs such as mediation, financial education, or the appointment of a trustee.
- **Performance of Clusters-** needs to be improved by
  - o Bringing **synergy and coordination** within large number of support schemes.
  - o Involving local intermediaries such as **business membership organizations** in developing linkages with other stakeholders such as training, educational and research institutions.
- **Market Support for MSMEs-** can be enhanced by developing networks of **development service providers** that can provide customized solutions to MSMEs that are struggling with capability and resources constraints.
- **Improving access to technology-** through a **technology Mission** for converging the efforts for the technology upgradation of the MSMEs. Apart from it more **Industry specific Technology Centres** can be opened.
- **Setup a National Council for MSMEs-** under the Chairmanship of the Prime Minister, in order to facilitate coherent policy outlook and unity of monitoring.

Recommendations for facilitating access to financing for MSMEs

- Banks should develop **customized products** to assess the financing requirements based on expected cash flows moving away from traditional forms of assessment.
- A second **Trade Receivables Discounting System (TReDS)** window can be created to solve the problem of delayed payments.
- Consider setting up of a **Non-Profit Special Purpose Vehicle (SPV)** to support crowd sourcing of investments by various agencies.
- **Small Industries Development Bank of India (SIDBI)-** should use **Priority Sector Shortfall (PSS) funds** for lending to State Governments as soft loans for infrastructural and cluster development. It should deepen credit markets for MSMEs in underserved districts and regions by handholding private lenders such as **Non-Banking Finance Companies** (NBFCs) and **Micro Finance Institutions** (MFIs).

Way Forward

The development of MSMEs is crucial on many counts for Indian economy and society. Apart from proper implementation of these recommendations, a cue could be taken from the global best practices such as the Competition by cooperation concept in Italy, Contract Financing in Mexico and success stories of Shenzhen as a technology hub in China.

8.2. SEZ POLICY REPORT

Why in news?

The **Baba Kalyani committee** constituted by the Ministry of Commerce & Industry to study the existing **SEZ policy** of India submitted its report to the government.

Performance of SEZ

- As on 31st March, 2018, there were a total of **223 Operational SEZs** against 355 notified SEZs in the country.
- **Total Investment** in SEZs (as on 31st March, 2018) amounted 4.75 lakh crore and it has generated close to **20 lakh jobs**.
- **Exports from SEZs** amounted nearly 5.81 lakh crore in 2017-18, which is higher from 5.23 lakh crore in 2016-17 and 4.67 lakh crore in 2015-16.

Major Challenges and Solutions

- **Unutilised land** (more than 25,000 hectares) in SEZs which is due to lack of flexibility to utilise land in SEZs for different sectors. The **solution to this challenge** is "Optimal utilisation of vacant land in SEZ by allowing flexibility of land use and removing sector-specific constraints."
- **Existence of multiple models of economic zones** such as SEZ, coastal economic zone, Delhi-Mumbai Industrial Corridor, National Investment and Manufacturing Zone, food park and textile park.

Special Economic Zone (SEZ) is a specifically delineated duty-free enclave and deemed to be foreign territory for the purposes of trade operations and duties and tariffs.
India's SEZ Policy was implemented from 1 April, 2000. Subsequently the Special Economic Zones Act, 2005 supported by SEZ Rules 2006.

The main objectives of the SEZ Act are:

- Generation of additional economic activity
- Promotion of exports of goods and services
- Promotion of investment from domestic and foreign sources
- Creation of employment opportunities
- Development of infrastructure facilities

The SEZ Rules provide for:

- Simplified procedures for development, operation, and maintenance of the Special Economic Zones and for setting up units and conducting business in SEZs;
- Single window clearance for setting up of an SEZ or a unit within it;
- Single Window clearance on matters relating to Central as well as State Governments;
- Simplified compliance procedures and documentation with an emphasis on self certification.
- **Approval mechanism and Administrative set up of SEZs:** The developer submits the proposal for establishment of SEZ to the **concerned State Government**. The State Government has to forward the proposal with its recommendation within 45 days from the date of receipt of such proposal to the Board of Approval. The **applicant also has the option to submit the proposal directly to the Board of Approval**.
- **The Board of Approval chaired by the Secretary, Department of Commerce** has been constituted by the Central Government in exercise of the powers conferred under the SEZ Act.
- All the decisions are taken in the Board of Approval by consensus.

The Special Economic Zones (Amendment) Bill, 2019

- It amends the Special Economic Zones Act, 2005 and replaces an Ordinance that was promulgated on March 2, 2019.
- Under the Act, the definition of a person includes an individual, a Hindu undivided family, a company, a co-operative society, a firm, or an association of persons. The Bill **adds two more categories** to this definition by including a trust, or any other entity which may be notified by the central government.

    - **Solution:** The group of secretaries of various central government's departments have recommended **"rationalisation"** of these models. Moreover, the Department of Industrial Policy and Promotion (DIPP) and the Niti Aayog is going to "develop and master plan for industrial clusters" in order to deal with this challenge.
- **Under-utilisation of existing capacity**. Currently, SEZ units are not allowed to do "job work" for domestic tariff area (DTA) units. Any area that lies outside of SEZ or any other custom bonded zone in India is known as the DTA. Goods and services going into the SEZ from DTA is treated as exports and goods coming from the SEZ into DTA is treated as imports. **It is recommended that** "optimal utilisation of existing capacity in SEZ units" should be done by "allowing job work for DTA".
- **Domestic sales of SEZs face a disadvantage** as "they have to pay full customs duty", as compared to the lower rates with the Association of Southeast Asian Nations (ASEAN) countries due to free-trade agreement (FTA). It is suggested that the "best FTA rates" should be allowed for domestic sales, too.
- **Imposition of Minimum Alternate Tax** (MAT) on SEZs from April 1, 2012, as well as **imposition of income tax on new SEZs and new units** from April 1, 2017 and April 1, 2020, respectively. The experts advocated restoration of income tax benefit as well as MAT exemption.
    - Also, there is a need to **align changed taxation regime under GST to the SEZ Rules**.
- Another challenge has been the "**requirement of payment in foreign exchange for services provided by SEZ units to DTA area**". To deal with this problem, it has been suggested an amendment in the definition of "services" in the SEZ Act, 2005.
- **Lack of support from the state government** when it comes to developing effective single-window system for clearances.
- **Other issues**: There are other demands of the business and industrial community. These include- grant infrastructure status to buildings of SEZs and industrial parks, permit external commercial borrowing (ECB) for entire SEZ infrastructure, allow a refinancing option through ECB; relax the "risk weightage norms" for the real estate sector.
    - Moreover, simplification of the process of granting environment clearance by the Union environment ministry and repeal of certain sections of the Urban Land Ceiling Act, 2007 is also demanded.
    - The Commerce ministry has been consistently lobbying with the finance ministry to exempt units in the SEZs from the minimum alternate tax, or MAT, imposed on them in 2011.

- Some of the incentives offered under the SEZ policy have been **challenged at the WTO by the US** and may need to be replaced by other sops.

Why China succeeded but India's SEZ had limited success?

There are eight distinguishing features which have contributed to the success of SEZs in China: Unique location, large size, investment friendly attitudes towards non-resident Chinese, attractive incentive packages, liberal Custom procedures, flexible labour laws, a strong domestic market and decentralisation of power in favour of provinces and local authorities for administering the zones.

- Chinese SEZs had **a geographic advantage** with most of the SEZs located near the ports unlike the Indian SEZ's that are more in the mainland. Of the five SEZs, Shenzhen, Shantou and Zhuhai are in the Guangdong province, adjacent to Hong Kong — the gateway to China.
- **Size** is another important factor for SEZ success in China. Each SEZ is well over 1,000 hectares, the minimum recommended area. In India, the EPZs converted into SEZs are not even a third of this.
- **Strong domestic market** is another important aspect for SEZ success unlike India where Policy impediments to sales in the domestic market hamper large domestic market potential.
- While in China the thrust of SEZs has been to attract **foreign investments and modern technology**, in India the emphasis has been on exports.
- **Decentralisation of power** was also a major reason for SEZ success in China. Provincial and local authorities were made partners and stakeholders, by delegating to them powers to approve foreign investment.
- The **hire-and-fire policy in SEZs** has been one of the biggest attractions for foreign investors in China. All jobs are on labour contract basis, which stand terminated upon the expiry of the terms, which can be fixed/flexible or for a specific job. In contrast, the labour policy in India is worker, rather than investment, oriented.

Recommendations of the Committee

- **Reincarnation of SEZs as employment and Economic Enclaves (3Es):** The main focus of the recommendations of the SEZ committee is on migration from export focus to economic and employment growth focus. For this to be achieved, incentives for the manufacturing SEZs have to be based on specific parameters including demand, investment, employment and technology, value addition and inclusivity.
- **Other supports for SEZ (3Es)**
    - Flexibility to enable 3E units to seamlessly support business outside the zone.
    - Supply of power directly to units from independent power producer (IPPs) at competitive rates to ensure uninterrupted power supply.
    - Fast tracking various approvals through online application process
    - Integrating MSMEs with the 3Es and giving additional incentives to zones focusing on priority industries
    - **Infrastructure status to 3E projects** to make cheaper finance available to them
- **Connectivity to remote SEZs:** Development of last mile and first mile connectivity infrastructure by government should be provided for land parcels which are far from highways and urban agglomerations.
- **Replicate Success of ITeS:** The success seen by services sector like IT and ITES has to be promoted in other services sector like health care, financial services, legal, repair and design services.
- **Tax benefits:** For services SEZs, **tax benefits must be retained** including extension of sunset clause, lowering taxes (such as a MAT of 9 per cent and exemption from DDT) for identified strategic services and allowing supplies to domestic market in Indian currency to bring parity between goods and services.
- **Ease of doing business:** The committee has advocated simpler entry and exit processes using time-bound online approval and dispute resolution through robust arbitration and commercial courts.
- **In line with WTO norms and the GST,** the Committee recommended to **prepare a sunrise list** for "focused diversification" such as engineering and design, biotech and healthcare services.
- **Align the policy framework to avoid competition among similar schemes** of industrial parks, export oriented units, SEZ, national investment and manufacturing zones and sectoral parks and provide ease of doing business to developers and tenants.

8.3. NATIONAL MINERAL POLICY 2019

Why in news?

The Union Cabinet has recently approved the National Mineral Policy, 2019 which aims at bringing about more effective regulation to the sector as well as a more sustainable approach while addressing the issues of those affected by mining.

Background

- National Mineral Policy 2019 replaces the extant National Mineral Policy 2008 in compliance with the directions of the Supreme Court in **Common Cause v/s Union of India & Others.**
- The Ministry of Mines constituted a committee under the chairmanship of **Dr. K Rajeswara Rao** to review the National Mineral Policy 2008.
- Based on the committee's report and subsequent deliberations with stakeholders, the ministry has finalized the policy.

Need of the review of Policy

- **Low rate of growth of Indian Mining sector**- with just 1-2 per cent contribution to GDP over the last decade (as opposed to 5 to 6 per cent in major mining economies).
- **Lack of focus on exploration**- the production vs import of minerals is in the ratio of 1:10 in India. High import is mainly because of non-availability of raw material for industries. Hence, exploration must be treated as a business and treating it as a startup giving tax holidays, tax benefits etc. to encourage investments for exploration.
- **Lack of incentives with private sector to invest**- Companies fear investing in exploring minerals owing to various risks.
- **Need to address illegality in mining and environmental concerns.**
- **Need to address concerns of intergenerational rights**

Salient features of National Mineral Policy 2019

- **Creation of dedicated mineral corridors** to **boost private sector** mining areas.
- **Granting status of industry to mining activity** to boost financing of mining for private sector and for acquisitions of mineral assets in other countries by private sector.
- **Long-term import export policy for mineral** will help private sector in better planning and stability in business.
- Introduces the concept of **Exclusive Mining Zones**, which will come with in-principle statutory clearances for grant of mining lease.
- **Introduces the concept of Inter-Generational Equity** that deals with the well-being not only of the present generation but also of the generations to come.
- **Utilization of the district mineral fund** for equitable development of project affected persons and areas.

Analysis of the Policy

Pros of the Policy

- **Business friendly policy**-which can help ramp up exploration and production. It aims to boost mineral production by 200% in next 7 years.
- **Provisions on sustainability**- as it talks about the inter-generational equity.

Cons of the Policy

- **Weak on environmental conservation**- the Policy only mentions is to use "renewable sources of energy at mining sites" to reduce pollution, carbon footprint and operational costs. It does not give guidance for specifying standards and outlining mechanisms for pollution monitoring in mining areas under the concerned laws.
- **Does not talk about entire value chain**- of new age minerals and acquire intellectual property on their extraction and downstream product development, while following the highest global standards of sustainable development.

Way Forward

There needs to be complete synergy among all stakeholders like industry, Central and state governments, regulators, so as to make the optimum use of this policy.

8.4. NATIONAL POLICY ON ELECTRONICS

Why in news?

The Union Cabinet has recently approved the National Policy on Electronics 2019 (NPE 2019).

Need for this new Policy

- **Evolving nature of Electronics Industry in India**- The implementation of the Schemes/ Programmes under the aegis of the **National Policy on Electronics 2012** (NPE 2012) has successfully consolidated the foundations for a competitive Indian ESDM value chain. Now, this NPE 2019 proposes to build on that foundation to propel the growth of ESDM industry in the country
- **Spillover effects of Electronics Industry**- such as growing security concerns, rising inverted duty structures, dependence on major powers and potential of job creation.
- Hence, Electronics is not just about a manufacturing of electronics as a consumable but electronics, which will have impact on working of every sector.

Mission and Objective the Policy

- The Policy envisions positioning India as a **global hub for Electronics System Design and Manufacturing - (ESDM)** by promoting domestic manufacturing, skill development, start-up, export eco-system and improving ease of doing business for the ESDM industry.
- It aims to achieve a turnover of $400 billion and generate 1 crore jobs in the ESDM sector by 2025.

Initiatives taken under NPE 2012

- **The Modified Special Incentive Package Scheme (M-SIPS),** launched in the wake of NPE 2012 offers subsidies for electronics industry. However, the rate of approval for applications filed and the investments made thereafter remain low.
- **The Electronics Manufacturing Clusters (EMC) Scheme,** launched in 2012, encouraged entities, including State Government entities, to provide good quality infrastructure within a cluster. Under the scheme, 50% of the project cost for Greenfield EMC and 75% for Brownfield EMC is given as grant.
- **The Electronics Development Fund (EDF) Scheme** was launched in order to promote startups and innovation. EDF is a Fund of Funds which invests in Venture Funds.

Strategy outlined in the NPE 2019

- **Creating eco-system for globally competitive ESDM sector-** by encouraging domestic manufacturing through consistent tax incentives, establishing **Electronic Manufacturing Clusters,** promoting Defence Offsets and sub-sectors like semi-conductor facilities, display fabrication units etc.
- **Promoting Ease-of-doing Business-** by facilitating single window mechanism for global investors using existing mechanisms like **Invest India**, **National Investment Promotion and Facilitation Agency.**
- **Encourage Industry-led R&D and Innovation-** in all sub-sectors of electronics. This would encompass support to various initiatives in areas like 5G, IoT/ Sensors, Artificial Intelligence etc. The support will include new Educational Courses, Incubation Centres, **Sovereign Patent Fund** and incorporate **principles of sustainability** of electronic goods through their life cycle.
- **Promote Trusted Electronics Value Chain-** to improve national cyber security profile and control its supply chain across **national defense** and **critical national infrastructure** like energy grids, communication networks, digital economy etc.
- **Developing Core Competencies in the sub-sectors of Electronics-** such as Indian Fabless Chip Design Industry, Medical Electronic Devices Industry, Automotive Electronics Industry etc.
- **Promotion of Electronic Components Manufacturing Ecosystem-** by providing incentives for lithium-ion cells, chip components, fuel cells, optical fibre, solar cells etc.
- **Preferential Market Access-** by encouraging states to adopt the Public Procurement (Preference to Make in India) Order 2017 (**PPO 2017**) and leveraging the **Government e-Market Place** (GeM) in the procurement of electronic products (including cyber security).
- **Other Measures-** Human Resource development, export promotion, Promoting Eco-park for e-Waste processing, **acquiring mines of Rare Earth Metals in foreign countries** (Africa, Australia) and developing an index to asses the status of electronics manufacturing industry in the states.

8.5. FOURTH INDUSTRIAL REVOLUTION

Why in News?

World Economic Forum launches **Centre for Fourth Industrial Revolution** in India.

Fourth Industrial Revolution and India

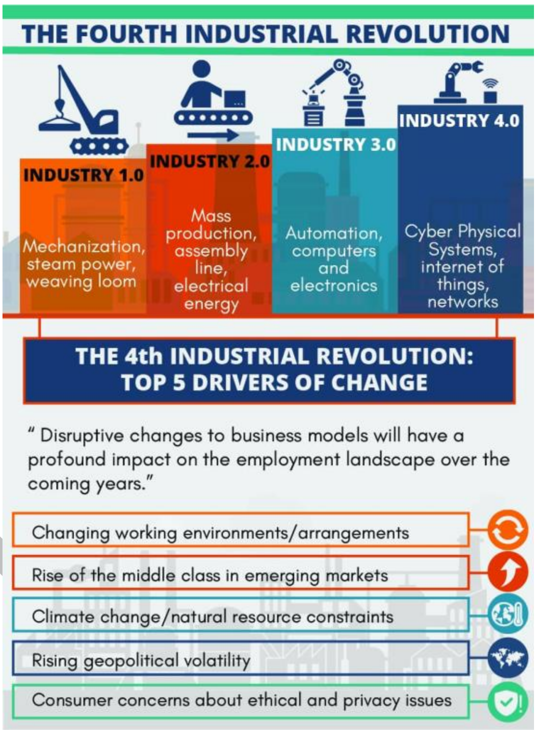
Opportunities

- India can play a pivotal role in shaping the global fourth Industrial revolution due to the benefits of a better **demographic dividend** (By 2020, the median age in India will be just 28, compared to 37 in China and the US).
- India can reap maximum **benefits of its expansion** in telecommunication sector, huge increase in data usage and availability due to government initiatives like Digital India campaign, Start-up India and the Atal Innovation Mission etc.
- **Artificial intelligence** (AI) can be used effectively to reduce poverty, improve the lives of farmers and make the lives of the differently abled simpler. AI has vast applications across sectors – ranging from medicine to criminal justice, to manufacturing, to finance.

- With the right mix of accelerators – including **regulatory frameworks**, **educational ecosystems** and **government incentives** – India can lead the Fourth Industrial Revolution while simultaneously enhancing the quality, equity and sustainability of its own growth and development outcomes.

Challenges

- Apart from shrinking jobs, India's large number of **low skilled youth** will also face major challenges in big industries as well as MSMEs because **product cycles will become very short** and this will lead to a lot of **uncertainty** and **unpredictability**.
- Small scale manufacturing faces deep **infrastructural problems** as well as **inadequate access to credit** which will be a hinderance in benefiting from the changes**.**
- The highly educated and technically skilled people will command huge salaries in large manufacturing enterprises using robotics and artificial intelligence which will create a huge income gap between the skilled and the unskilled workforce.



Way forward

With the right mix of accelerators - including **regulatory frameworks, educational ecosystems and government incentives** - India can lead the fourth industrial revolution, while simultaneously enhancing the quality, equity and sustainability of its own growth and development outcomes. Among various steps required, following are some important ones-

- Companies should **invest in their technical infrastructure and data analysing capabilities**. All businesses must be making a move to be smart, connected organizations or they will soon fall behind the competition.
- **Education and training systems** need to adapt to better prepare people for the flexibility and critical thinking skills they will need in the future workplace.
- India needs to strike the right balance between vocational and **new digital industrial skills**, boosting **education in data science and coding** but also providing greater training in **traditional manufacturing skills.**
- India must take a pragmatic approach to quickly **boost traditional manufacturing** while **adopting new digital industrial technologies** that will secure long-term competitiveness.

8.6. SOLAR MANUFACTURING IN INDIA

Why in News?

Recently, there has been a view among experts, that India needs a **Solar Manufacturing Strategy**, if it wants to achieve its ambitious Solar Program.

Background

- India has made significant progress in creating capacity for solar energy generation in the last few years. India expanded its solar generation capacity eight times from **2,650 MW** in 2014 to **28.18 GW** on March 31, 2019.
- The government had an initial target of 20 GW of solar capacity by 2022, which was achieved four years ahead of schedule. In 2015, the target was raised to 100 GW of solar capacity by 2022.
- Despite the new policy focus on solar plant installation, India is **still not a solar panel manufacturer**.

Issues in Solar Manufacturing in India

- **Overdependence on low-cost imports-** India met 92.11 per cent requirement of its solar equipment through imports in 2017-18.
    - China is the largest supplier of solar equipment accounting for about 89 per cent of India's total imports of solar cells in 2017-18.

Potential of Solar Manufacturing in India

- **Employment generation:** It has a potential to create 50,000 direct jobs and at least 125,000 indirect jobs in the next 5 years.
- **Reduction in imports:** Domestic solar manufacturing can save USD 42 bn. in equipment imports by 2030, besides providing equipment supply security.
- **Domestic demand:** India's large demand (planned solar power growth) in the coming years is the perfect opportunity to build a domestic manufacturing base for equipment (panels and cells) and scale them up much like China did.
    - According to the Ministry of New and Renewable Energy (2018), India has an annual solar cell manufacturing capacity of about 3 GW while the **average annual demand is 20 GW**.
- **Expanding overseas market:** India has taken a lead in the **International Solar Alliance** (ISA), which will help in the transfer of solar technologies across members.
    - India also sees this as an opportunity for the domestic solar industry to find inroads in some of the smaller and untapped markets like Africa and South America.

- **Lack of a manufacturing base** for Poly-silicon, Ingots/wafers, the upstream stages of solar PV manufacturing chain, which is a very energy intensive process. Most Indian companies are engaged in only module assembly or wafer manufacturing and module assembly.
- **Higher cost of production**- due to lack of integrated set up, economies of scale & modern technology.
    - Also, the domestic manufactures have to borrow at higher interest rates, compared to foreign manufacturers, pushing up their cost of production.
    - Thus, the price of solar equipment produced in the country is not competitive as compared to that of foreign manufacturers.

Concept Note on Solar PV Manufacturing Scheme by Ministry of New and Renewable Energy

- To create end-to-end solar PV manufacturing capacity in India by way of building up manufacturing capacity of solar PV modules, cells, wafers/ ingots and polysilicon in India.
- To convert India from a net importer country to a net exporter country and becoming a global player in solar manufacturing.

- **Government's attempts faced different challenges-**
    - India's attempt to provide a leg-up to local manufacturers through **Domestic Content Requirement** was thwarted when World Trade Organisation overruled the local sourcing requirements on imports placed by the Government.
    - In 2018, India imposed a **Safeguard Duty** on imported solar panels.
        - ✓ While imposition of this duty was aimed at incentivising domestic manufacturing, it led to **an increase in tariffs,** resulting in the cancellation of many solar auctions.
        - ✓ But, for Indian manufacturers, protection from the safeguard duty soon disappeared since Chinese panel manufacturers also reduced the module prices.
- **Other regulatory issues**- such as high cost of land/ electricity, low capacity utilization, and lack of skilled workforce. These along with the aforementioned issues have led to a poor response from industries.

Steps taken by Government

- India's Manufacturing Policy recognizes solar manufacturing as an industry with '**strategic importance**'.
- One of the objectives of the **National Solar Mission** is "to create favourable conditions for solar manufacturing capacity, particularly solar thermal, for indigenous production and market leadership".
- In the **solar panel manufacturing sector**, the Indian government **allows 100% foreign investment** as equity and it qualifies for automatic approval.
- The government is also encouraging foreign investors to set up renewable energy-based power generation projects on build-own-operate basis.
- A 25 percent capital subsidy for solar manufacturing units is available under the '**Modified Special Incentives Package Scheme'** (M-SIPS).
- The Cabinet Committee on Economic Affairs (CCEA) approved a **viability gap funding (VGF) scheme** worth Rs. 8,580 crore, which would enable government-owned companies to set up 12 GW of solar power plants over the next four years using the costlier, made-in-India modules.

Measures, which need to be taken

- **India needs a solar manufacturing strategy**, on the lines of the Automotive Mission Plan (2006-2016), which is credited with making India one of the largest manufacturers of automobiles in the world. A right policy framework with well-defined objectives will help India set up a robust PV manufacturing ecosystem.
- **Focus on large-scale public procurement**- The government can call out bids for solar power plants with the requirement that these be made fully in India. This will not violate any WTO commitment.

- **Cluster Approach-** Globally, manufacturing bases are being planned as integrated solar industrial clusters with strong Government support. A SEZ that focuses only on integrated module manufacturing could be planned to create a conducive environment.
- **Ideas which can be adopted from China-**
  - **Develop 'Solar Champions'**- in a systematic manner through massive subsidies, low interest loans, grants and easy access to land and utilities.
  - The Technology Top Runner Program- which aims to achieve higher-efficiency solar products for 1.5 GW of next-generation PV technology. Through such targets, China is able to drive mass production of cells.

8.7. TECHNICAL TEXTILES

Why in News?

National Conclave on Technical Textiles was held recently in Mumbai.

What are technical textiles?

- These are **textile material and products manufactured primarily for technical performance and functional properties** rather than aesthetic and decorative characteristics.
- They find application not only in clothing but also in areas like agriculture, medical, infrastructure, automotive, aerospace, sports, defence and packaging.
- Based on usage, there are 12 technical textile segemts. Examples- Agrotech (fishing nets), meditech (sanitary napkins) etc.
- It is a **sunshine sector** for the textile industry and it is one of the fastest growing segments of the Indian Economy. They are driven by demand, development and industrialisation in a country. In India, most units are concentrated in Gujarat.
- This industry is **import-intensive**. In the last few years, the industry has witnessed a rise in imports - it stood at USD 1.4 Billion in 2014-15.

Textile Sector in India

- **Biggest employer after agriculture** employing 4.5 crore people directly.
- Indian textile industry, **the 2nd largest manufacturer and exporter in the world**, contributes 12.65 % to manufacturing and 2.3 % to GDP.
- India has a **share of 5% of the global trade** in textiles and apparel.
- The share of textile in India's total exports stands at 12 per cent (2018-19).
- It plays a **critical role in improving social dynamics** as mostly women are employed in the sector.
- The backward linkages of the sector to the rural economy give huge opportunities to millions of farmers, artisans, handloom and handicraft manufacturers.
- The sector is perfectly aligned with Government's key initiatives viz., Make in India, Skill India, etc.
- **Some of the challenges faced by this sector-**
  - Absence of scale or fragmented and scattered manufacturing.
  - While the ginning and spinning sectors are on par with international standards, marginal technological gap exists in weaving, processing and embroidery.
  - Indian exports of apparel continue to face higher average tariffs in external markets as compared with competing nations which enjoy duty free access.

Government initiatives for this sector

- Government launched **Scheme for growth and development of technical textiles** (SGDTT). Its 3 components were:
  - Baseline survey to build technical textile industry database.
  - Setup centres of excellence for infrastructural support.
  - Awareness generation among entrepreneurs.
- Subsequently, government launched **Technology Mission on Technical Textiles (2010-2014)** for standardization and export promotion.
- All technical textiles-based machinery is covered under **Technology Upgradation Fund Scheme,** which facilitates new and appropriate technology for making the textile industry globally competitive.
- Government has allowed up to **100% FDI under automatic route** for the technical textiles segment.

9. SERVICES SECTOR

9.1. DRAFT E-COMMERCE POLICY

Why in news?

The government released the draft e-Commerce policy.

Need for an E-Commerce policy

- **Data Ownership:** In the age of e-Commerce, companies control large amounts of customer data. The questions, related to control of an individual over his own data or government accessing the data of its citizens, need to be answered.
- **Rapid growth of e commerce**: The Indian B2C e-commerce market was valued at $38.5 bn in 2017 and is estimated to rise to $200 bn in 2026, while B2B e-commerce was estimated to be around $300 bn. Its export potential too has not been realized. Thus, the rules for electronic commerce in the country must be clearly laid-down.
- **Presence of multiple regulators:** The specific issues in e-Commerce are the subject matter of different statutes - Information Technology Act 2000, Competition Act 2002, Consumer Protection Act 1986 etc. – and involves multiple government departments. Hence, a national e-commerce policy would consolidate the various norms and regulations to cover all stakeholders.
- **Other regulatory issues:** Government is finding existing regulations inadequate to deal with issues thrown up by the digital economy. For instance, authorities cannot impose 'custom duty' on digital transactions. Regulators find it difficult to hold entities responsible that have physical presence abroad.
- **Consumer Protection:** A strong regulatory regime would address the issues of frauds in online sale and protect the interest of consumers.
- **Digital Infrastructure:** There is a lack of requisite connectivity required for e-Commerce & digital literacy in many parts of the country. New e-Commerce policy will address such structural issues.
- **Inequality in opportunity among businesses:** Enterprises with deep pockets indulge in **large scale capital dumping** to finance sustained selling at losses, which has threatened existence of small businesses. A policy is needed to provide a level-playing field to all stakeholders, including consumers, MSMEs & start-ups.
- **International Trade Outlook:** A new policy will preempt any possible obligations on e-commerce imposed by WTO. Creating binding obligations, like permanent moratorium on imposing customs duties on electronic transmissions, would lead to loss in revenue of developing countries like India.

Strategy proposed in the draft policy

- **Data:** It acknowledges the importance of data as a **'national asset'/ 'societal common'** and seeks to establish a legal & technological framework to **restrict cross-border flow of data** generated in India.
- **Infrastructure Development:** It recommends according **'infrastructure status' to supporting digital infrastructure** like data centres, server farms for data storage etc. Also, **domestic alternatives to foreign-based clouds** and email facilities should be promoted.
- **E-Commerce Marketplaces**
  - **FDI Policy:** The policy aims to clearly **demarcate between a marketplace model** & **an inventory-based model** and seeks to encourage FDI in the 'marketplace' model alone.
- **Regulatory Issues**
  - **Inter-disciplinary nature of e-commerce:** Standing Group of Secretaries on E-Commerce (SGoS) should tackle specific issues emerging under different statutes, give recommendations to address policy challenges & ensure that the policy keeps pace with the digital environment.
  - **Controlling data flow & network:** Regulation of advertising charges in e-commerce, especially for MSMEs & start-ups. To seek better accountability in situations of AI-driven decision making, the government must reserve its **right to seek disclosure of source code & algorithms**.

Issues with the new policy

- **Treating individual's data as a collective property** and national asset that the government holds in trust for its citizens implies that the government does not trust its citizens to make the right choices about their personal data. This is **in contradiction with the recommendations of the Justice Srikrishna committee and SC's decision in its right to privacy judgement.**
- Many Indian companies use the facilities of cloud-based storages and solutions like Amazon Web Services (AWS). **Mandating these companies to store in locally will affect their operational cost and efficiency.**

- Law & Order: Access to data for maintenance of law & order must be allowed.
  - **Small enterprises and start-ups:** Small firms and start-ups attempting to enter the digital sector can be given **'infant-industry'** status.
  - **Taxation Issues:** The concept of **'significant economic presence'** should be adopted as the basis for determining **'permanent establishment'** for the purpose of taxation. Additionally, the current **practice of not imposing custom duties on electronic transmissions** must be reviewed in light of the changing digital economy.
  - **Content Liability:** Online platforms and social media ('intermediaries') must bear the responsibility & liability to ensure genuineness of any information posted on their websites.

Models of E-Commerce

Marketplace Model
- E-commerce Company provides an IT platform on a digital or electronic network to act as facilitator between buyers & sellers without warehousing the products.
- It aggregates various retailers/brands and provide a sales channel (offers shipment, call centre, delivery and payment services) to them but cannot exercise ownership of the inventory.
- It allows for a superior customer service experience, as many smaller brands have greater outreach now, with their fulfillment processes taken care of by online marketplaces. E.g. E-Bay/Shopclues etc.
- 100% FDI is allowed in marketplace model of e-commerce.

Inventory Model
- Products are owned by the online shopping company. The whole process end-to-end, starting with product purchase, warehousing and ending with product dispatch, is taken care of by the company.
- Allows speedier delivery, better quality control and improved customer experience and trust. But, it restricts cash flow and is difficult to scale
- FDI in multi-brand retail is prohibited, including e-commerce retail (B2C);
- E.g. Jabong, YepMe etc.

- **Stimulating the Domestic Digital Economy:** It intends to **increase use of internet** in day-to-day governance and economy. E.g. automating logistics sector through online customs clearance & adopting Customs Electronic Data Interchange (EDI) platform.
- **Export Promotion Through E-Commerce:** The transaction procedures must be simplified to increase competitiveness of e-commerce exports

9.2. NATIONAL POLICY FOR SOFTWARE PRODUCTS

Why in news?

The Union Cabinet has recently approved a national policy on software products which aims to position India as a Software Product nation and create 65 lakh jobs by 2025.

Need of a New Policy

- As per **NASSCOM Strategic Review 2017,** the Global Software Product Industry is estimated to be **USD 413 billion.** However, the contribution of Software Products in Indian IT-ITES revenue is just USD 7.1 billion out of which 2.3 billion USD are exports.
- On the other hand, import of Software Products is estimated to be nearly 10 billion USD, so as such India is a **net importer of software products** at present.
- Also, past few years have seen serious decline in growth, owing to **rapid transformation in technology and Software industry**, globally.
- **The first Software policy came up in 1986.** However, as a maturing industry, with a distinct and strong charter of growth, there is a need to reevaluate the sector and to draw out strategies with a medium to long term perspective and **introduce innovative solutions to leverage its full potential.**
- There is a need to address weaknesses in regard to developing innovative software products that **address the challenges thrown in implementing ambitious programmes** like Digital India, Make in India, Smart cities etc.

Strategies of National Policy for Software Products

- **Promoting Software Products Business Ecosystem by**
  - Creation of an Indian Software Product Registry
  - Facilitating active participation of software companies in Capital Market
  - Creation of a Single Window Platform

- **Promoting Entrepreneurship & Innovation for Employment by**
  - Initiating a programme of incubation
  - Initiating a Programme to support Research and Innovation on Software Products in Institutes of Higher Learning and Research
  - Creating domain specific Indian software product clusters
  - Creating a dedicated Software Product Development Fund (SPDF)
- **Skilling and Human Resource Development by**
  - Initiating a national "Talent Accelerator" programme- to motivate school and college students.
  - Creating a talent pool of 10,000 committed software product leaders
- **Improving Access to Domestic Market and Cross Border Trade Promotion by**
  - Integrating the registry of Indian software products with Government e-market (GeM)
  - Encouraging Indian Product Startups/ MSMEs through hackathons.
  - Promoting implementation of open Application Program Interface (APIs) proactively
  - Promoting preferential inclusion of Indian software product in Government procurement
  - Overcoming language barriers
- **Implementation Mechanism such as**
  - Establish a "National Software Product Mission (NSPM)"
  - Include various Ministry of Electronics and Information Technology's organizations in the implementation- such as Software Technology Parks of India (STPI)

Five Missions of the Policy

- To promote the creation of a sustainable Indian software product industry, driven by intellectual property (IP), leading to a ten-fold increase in share of the Global Software product market by 2025.
- To nurture 10,000 technology startups in software product industry, including 1000 such technology startups in Tier-II and Tier-III towns & cities and generating direct and in-direct employment for 3.5 million people by 2025.
- To create a talent pool for software product industry through
  - Up-skilling of 1,000,000 IT professionals,
  - Motivating 100,000 school and college students
  - Specialise 10,000 professionals that can provide leadership.
- To build a cluster-based innovation driven ecosystem by developing 20 sectoral and strategically located software product development clusters having integrated ICT infrastructure, marketing, incubation, R&D/test beds and mentoring support.
- In order to evolve and monitor schemes & programmes for the implementation of this policy, National Software Products Mission will be set up with participation from Government, Academia and Industry.

9.3. NATIONAL DIGITAL COMMUNICATIONS POLICY 2018

Why in News?

Recently, Union Cabinet approved the **National Digital Communications Policy-2018 (NDCP-2018)** and re-designated Telecom Commission as the **"Digital Communications Commission"**.

Telecom Commission (now Digital Communications Commission)

It was set up by the Government of India via resolution to deal with various aspects of Telecommunications. The Telecom Commission is responsible for:

- Formulating the policy of Department of Telecommunications for approval of the Government;
- Preparing the budget for the Department of Telecommunications for each financial year and getting it approved by the Government; &
- Implementation of Government's policy in all matters concerning telecommunication.

Need of the new policy:

- NDCP– 2018 has been formulated to cater to the needs of **modern technological advancements** in the Telecom Sector such as – 5G, IoT, Machine to Machine (M2M) learning, etc. that required a 'customer focused' and 'application driven' policy for the Indian Telecom Sector.
- It seeks to overcome shortcomings of previous **National Telecom Policy, 2012** in areas such as enhancing rural tele-density, optical fibre network to gram Panchayats, minimum broadband speed, etc.
- This policy can form the main pillar of **Digital India** by addressing emerging opportunities for expanding the availability of Telecom services and also Telecom based services.
- Through NDCP-2018 government wants to focus on **socio-economic growth** of the country with the help of the telecom sector instead of seeing it as source of revenue generation.

Strategies for Three Missions

1. Connect India

- Establishing a '**National Broadband Mission – Rashtriya Broadband Abhiyan**'
- **Recognizing Spectrum as a key natural resource**
- **Strengthening Satellite Communication Technologies**
  - Optimise Satellite communications technologies in India, by **reviewing SATCOM policy**
  - **Making available new spectrum bands**
  - Develop an **ecosystem for satellite communications** in India, with focus on: Promoting participation of private players
- Ensuring Inclusion of uncovered areas and digitally deprived segments of society by **channelizing the Universal Service Obligation Fund (USOF).**

2. Propel India

- Catalysing Investments for Digital Communications sector by according Telecom Infrastructure the **status of Critical and Essential Infrastructure**
- Ensuring a holistic and harmonised approach for harnessing Emerging Technologies
- Focussing on R&D by **creating a Fund for R&D**
- **Local Manufacturing and Value Addition**
- Other strategies include Capacity building, strengthening of PSUs, create a **roadmap for transition to Industry 4.0** by 2020 etc.

3. Secure India

- Core strategies include establishing a strong, flexible and robust **Data Protection Regime**
- Developing a **comprehensive plan for network preparedness, disaster response relief, restoration and reconstruction**

Significance

- The essence of the NDCP lies in its innate vision to transform the face of India's ICT industry by leveraging the principles of Design, Innovation and Creativity-led Entrepreneurship (DICE).
- It is praiseworthy to note that this policy focuses on end-to-end solutions along the entire ICT value chain under the core themes of 'Connect India, Propel India and Secure India'.

9.4. REAL ESTATE INVESTMENT TRUST

Why in News?

Blackstone Group along with Embassy Office Parks has filed India's first and Asia's largest prospectus for Real Estate Investment Trust (REIT).

What is a REIT?

- **REITs are listed entities which owns, operates and manages buildings/properties** (like Office Parks, Malls, Hotels, Residential Buildings etc.) for generating income and is bound by norms defined by SEBI and RERA, 2016.
- But **REITs functions like a mutual fund** and raises money from a number of investors and issues dividends to investors as return.

Benefits of REITs

- **Bring more investments:** REITs will facilitate more investment in the real estate sector – both domestic and foreign investment by bringing **transparency in asset valuation and financial transparency practices etc.**
- **Philip to real estate sector**: REITs can purposefully step up funding for India's woefully underfunded urban real estate, including to utilise the scope for city redevelopment, and also provide attractive, stable and long-term returns for retail investors.
- **Good option for small investors:** This means that you can add real estate to your investment portfolio without worrying about huge loans.
- **Diversification of portfolio**: REITs would also enable diversification of the portfolio of the investors and

provide the investors a new product that is regular income generating.

- It also gives developers an **option to exit projects**, including those developers who are reeling under a financial crunch.

Problems with REITs

- While RERA was enacted in 2016, the first REIT listing happened recently even after several relaxations in regulations by SEBI due to the lack of confidence of investors in real estate sector in India.

> **Real Estate (Regulation and Development) (RERA) Act** was enacted in 2016. Features of RERA, 2016:
> - Intends to **regulate transactions between buyers and promoters** of residential and commercial real estate developers.
> - Creation of Real Estate Regulatory Authority
> - Creation of Real Estate Appellate Tribunals to hear appeals against RERA
> - Promoter has to maintain a 'separate account' for every project undertaken
> - Promoter has to deliver projects in a time bound manner

- The minimum REIT investment amount has been set at a high value of Rs. 2 lacs. This deters the retail investors from investing in REITs.
- As land comes under state list, the legal status of REITs in some states is ambiguous.

9.5. PRICING OF DRUGS

Why in news?

Recently, a Parliamentary Standing Committee on Chemical and Fertilizers submitted its report on the subject "Pricing of Drugs with special reference to Drugs (Prices Control) Order, 2013".

Need for controlling the drug prices

- According to NSSO's 71st round survey (2014), around 72% in rural areas & 68% in urban areas of the total medical expenditure was incurred for purchasing medicines. Hence, the **affordability of medicines** is a crucial element in availing medical treatment by all sections of the people.

> **Principles of NPPP**
> - **Essentiality of Drugs:** Regulation of prices of drugs is on the basis of essentiality of drugs as per NLEM
> - **Control of Formulations prices only:** Only the prices of formulations (i.e., medicines used by consumers and not applicable to any upstream products such as bulk drugs or intermediaries) are to be regulated and not the prices of the Bulk Drugs (unlike Drug Policy of 1994).
> - **Market Based Pricing:** Ceiling price is calculated based on 'market data' wherein Average Price to Retailer & local taxes are considered for pricing.
>
> **Features of NPPP**
> - **Methodology of price fixation:** Ceiling prices of essential drugs is fixed based on simple average of the prices of all brands of the drug (in a particular therapeutic segment), which have at least 1% market share.
> - **Revision of prices:** Ceiling prices of scheduled medicines are allowed an annual increase as per the Wholesale Price Index (WPI)
> - **Non-scheduled formulations:** Non-scheduled medicines are allowed a price increase of 10% per annum only, to control the overall prices of drugs.
> - **No separate price for imported drugs** (if mentioned in Schedule 1 of DPCO).

- Insurance covers only hospitalization bills and not the cost of drugs. More than **2/3rd of Out-of-Pocket expenditure is incurred on drugs**.
- There is a **lack of awareness among the public about the free supply** of drugs by the Government as well as generic drugs. There exists a nexus between medical practitioners, chemists & pharmaceutical companies.

Development of Price Control Regime in India

- Drugs (Price Control) Orders [DPCO] under **Essential Commodities Act 1955** aim to regulate the prices of bulk drugs and their formulations to make them more affordable.
- Initially, **Drug (Price Control) Orders** focussed primarily on limiting the overall profitability through **cost-based pricing**.
- **National Pharmaceutical Pricing Policy 2012** put in place a regulatory framework for pricing of drugs to ensure availability of essential medicines at reasonable prices even while providing sufficient opportunity for innovation & competition to support the growth of industry.
  - National Pharmaceutical Pricing Policy (NPPP) is the policy governing price control and DPCO is the order by which price control is enforced.
  - NPPP was implemented through **Drugs (Prices Control) Order 2013 [DPCO 2013]**. The list of essential medicines, along with dosages & strengths, are included in **Schedule-1** of DPCO & are subject to price ceilings.

- Under current mechanism, the Health Ministry draws up a **National List of Essential Medicines** (NLEM). Under **NLEM 2015**, a total 376 drugs are under price control.
- On the basis of the NLEM, **National Pharmaceutical Pricing Authority (NPPA)** fixes prices of formulations using the provisions of the DPCO and monitors its compliance.
  - All essential medicines (as defined under NLEM) are treated as scheduled formulations (under DPCO-2013). However, it does not mean that all drugs brought under price control are essential medicines

National Pharmaceutical Pricing Agency
- It is an **independent, executive body of experts** under **Ministry of Chemicals and Fertilizers** formed in **1997**.
- Its primary function is to fix & revise the prices of scheduled formulations under the Drugs (Prices Control) Order (DPCO).
- It also undertakes monitoring and enforcement of prices of scheduled drugs through market surveillance
  - Purchase of samples by NPPA officers all over India to ensure compliance
  - Examine complaints by individuals / NGOs
- Failure to adhere to price limits makes companies liable to refund excess amount to NPPA.
- NPPA also provides inputs to Government on pharmaceutical policy and issues related to affordability, availability and accessibility of medicines.

- In addition, the following safeguards were provided in **Drug Price Control Order, 2013 to ensure effective control & regulation** in price movement of scheduled & non-scheduled medicines and availability of the essential medicines:
  - The government has the power to bring any item of medical necessity under price control in public interest. This provision has been used to cap the prices of cardiac stents and knee implants.
  - The manufacturers selling scheduled formulations below the ceiling price are to maintain the sub-ceiling price.
  - The manufacturers proposing to produce a new combination/ strength/ dosage form of the Schedule 1 medicines need to take price approval before selling it.
  - The manufacturers have to take permission of the Government before discontinuing the manufacture of essential medicines.

Bulk drug or Active pharmaceutical ingredients (API)- means any pharmaceutical, chemical, biological or plant product including its salts, esters, isomers, analogues and derivatives, conforming to standards specified in the Drugs and Cosmetics Act, 1940 and which is used as such or as an ingredient in any formulation.
Formulation - means a medicine processed out of or containing one or more drugs with or without use of any pharmaceutical aids, for internal or external use for or in the diagnosis, treatment, mitigation or prevention of disease and, but shall not include any AYUSH medicine.

- It is pertinent to note that the **Drugs & Cosmetics Act, 1940** administered by the Ministry of Health and Family Welfare do not contain any provisions for pricing of drugs.

Why market-based pricing mechanism was introduced in DPCO, 2013?

Prior to 2013, the DPCO followed a cost-based pricing mechanism that was based on the **costs involved in manufacturing a medicine along with reasonable profit margins**. But, such a mechanism suffers from following flaws:

- **Difficult to put a reasonable limit on the profit margin:** In Pharma industry, the process of discovering a new drug involves a long process of attrition, where hundreds of compounds might trickle down to one or two medicines. Thus, research & development of new drugs takes a lot of time and incur huge cost and must be appropriately incentivized.
- **Different cost of inputs:** The same drug can be manufactured by many companies of different scale and thus, will have different cost of inputs. It is difficult to maintain uniformity in cost-based calculation of price.
- **Problems in auditing cost:** Many companies don't divulge the actual costs incurred in the manufacturing process for competitive reasons. The process of verification may lead to intrusive inspector raj and increase red-tapism.

Thus, the government has decided to go for market based pricing to bring in more transparency and to encourage innovation and research in the field.

Prevailing issues in Drug Price Control regime in India

- **Reduced supply of essential drugs:** Price ceilings makes manufacturing of scheduled drugs unprofitable, so many pharmaceutical companies are moving to manufacture non-scheduled drugs especially smaller companies. This has dried up the supply side for many essential drugs. E.g.

- Supplies of Furoped (a life-saving drug for children with heart ailments) had come down by almost 40% after NPPA had imposed a price ceiling.
- Similar arguments have been raised against capping of prices of cardiac stents and knee implants.

- **Lack of control over non-essential drugs:** NPPA doesn't have pricing control in case of non-essential drugs, which comprise around 90% of domestic Pharma sales. Many drugs needed against life threatening diseases such as breast cancer are not included.
- **Nexus between Pharma companies and Hospitals:** Hospitals overcharge for treatment within their facilities, not allowing patients to source drugs independently from distributors. Pharma companies keep the retail price of drug high but offer huge cut to hospitals for prescribing their brands

Recommendations of the Committee

- **National Essential List of Medicines:**
  - The present nomenclature of NLEM is not appropriate and may be reviewed & suitably modified.
  - Moreover, the existing list of essential & life-saving medicines must be enlarged.
  - Also, permanent representation should be given to NPPA in the core committee on to review and revise the National List of essential Medicines (NLEM).
- **Market based pricing:** An expert committee should be constituted to study the impact of market based and cost based pricing systems on drug prices in the country.
  - Many health experts suggest that cost based pricing would actually make the drugs cheaper.
- **Jan Aaushadhi Stores:** More functional Jan Aaushadhi stores should be opened in all districts and supply chain should be improved by appointing distributors and Carrying & Forwarding (C&F) agents. Awareness among people about **Pradhan Mantri Bharatiya Janaushadhi Pariyojana** (PMBJP) scheme should be increased.
- **Generic Drugs:** Doctors should be advised to prescribe generic name of the drug instead of the brand name.
- **Stringent Penal Provisions:** If the manufacturer does not refund the excess amount (charged above the ceiling price) within the prescribed time limit given by NPPA, cancellation of licenses of such companies may be considered. Similar action may also be taken on retailers who indulge in overcharging of drugs/medical devices.
- **Better Quality Control:** Adequate measures should be taken to considerably increase the number of samples of drugs to be tested to better identify and curb the sale/distribution of spurious/non-standard quality drugs. There is also urgent need for time bound decision on the prosecutions launched against manufacture, sale and distribution of spurious/non-standard quality drugs.
- **Composition of NPPA:** The current composition of NPPA needs to be expanded to include more full time expert members so that administrative efficiency of the organization is enhanced.

10. INFRASTRUCTURE

Introduction

- As per industry estimates, infrastructure in India needs an investment of **USD 6 Trillion in the period 2016**-2030.
- However, Indian infrastructure sector has faced **several challenges** such as: cost and time over-runs in projects, inappropriate risks sharing through PPP framework, uncertainty in the policy and regulatory frameworks, prolonged disputes between Government and Private players, as well as sectoral issues including poor financial health of public sector counter party entities such as the power discos etc.
- Further, the sector **faces critical financing issues** in terms of high cost of capital, challenges in obtaining non-recourse funding and dearth of long-term funding sources due to the asset liability mismatch.
- Moreover, significant investment in the Indian infrastructure sector by domestic investors is also stuck due to well documented challenges and problems persistent in the sector.
- These issues have **adversely impacted the commercial viability of the projects**. As a result, the sector is marred with sluggishness in financing with further aggravation due to the **unprecedented stress levels** in the banking sector on account of increasing **Net NPAs**, which reached a level of 4.6% (2017).
- To address the challenges faced by the sector, important recommendations were made by the Committee on Financing Infrastructure chaired by **Mr. Deepak Parekh**. It has made recommendations to enhance the infrastructure financing by tapping additional avenues from domestic and international sources and by enriching the financing in terms of better risk recognition, longer tenure and lower cost of debt.
- Further, there is a need for implementing a comprehensive strategy for addressing the issue of infrastructure financing in India involving efficient and innovative financing mechanisms.

10.1. DRAFT NATIONAL URBAN POLICY FRAMEWORK

Why in news?

The Ministry of Housing and Urban Affairs released its first draft of the **National Urban Policy Framework (NUPF), 2018.**

10 Urban Sutras (Principles) of NUPF

- Cities are clusters of human capital
- Cities require a 'sense of place
- Not static Master Plans but evolving ecosystems
- Build for density
- Public spaces that encourage social interactions
- Multi-modal public transport backbone
- Environmental sustainability
- Financially self-reliant
- Cities require clear unified leadership
- Cities as engines of regional growth.

Background

- India has been urbanized at a fast pace in the last two decades, yet despite many efforts, India's cities are struggling to provide for their current population. This shows an urgent need to revisit the country's urban strategy.
- Building both on the international frameworks as well as the national missions, the **National Urban Policy Framework (NUPF)** outlines an integrated and coherent approach towards the future of urban planning in India.
- The NUPF is **structured along two lines:** (i) 10 **core philosophical principles** of urban planning, and (ii) these principles are then applied to **ten functional areas** of urban space and management.
- The framework provides recommendations on these functional areas.

Key Challenges and Recommendations

Functional Area	Challenges	Recommendations
City Planning	• Master planning has led to a static built environment, which is largely disconnected from the rapidly changing socio-economic conditions in urban areas • Master plans fail to be truly comprehensive due to the missing link between the spatial and functional aspect • Urban planning has been done with the male perspective.	• Planning area boundaries must include both **urban and peri-urban areas** • Master plans should be **dynamic** and stipulate clear links to budgets. • Spatial planning exercise should be participatory and ensure that it embraces diverse views of all sections of the society • Master planning should be made more efficient using technologies like GIS, GPS, Remote sensing etc.

Urban Economy	• Congestion effects are preventing realization of full economic potential of urbanization • Urban development in India has remained isolated from planned national development	• Cities instead of remaining isolated centres of economic activity with weak linkages to hinterland should become vibrant centres and make full use of natural and human resources in the regions • The states should develop strategies on how to integrate the informal sector into the economic system both in terms of space but also input and output linkages. • Explore new avenues of job creation in green technologies, new and eco-friendly construction methods. • In larger cities, City Economic Councils can serve as a clearing house between business and governments to hasten progress of specific projects. • A quarterly City Dashboard capturing city-level investments, GDP and employment growth
Physical Infrastructure	• **Drinking Water** o Source of water far away o inordinate dependence on sub-surface water o governments are unwilling to pass on the actual costs to consumers • **Sanitation and sewerage** o Lack of investments on improving or even maintaining the standards o large parts of cities are not covered to sewerage disposal systems; wastes find their way into rivers	• **Value Capture Finance Framework** (e.g. tax increment financing). • Professional institutions for each of the areas of urban infrastructure governance. • States should improve efficiency and service delivery over a period of time by switching over to performance-based contracts, as in Nagpur. • Use integrated digital technologies • **Integrate spatial plans with infrastructure plans**.
Social Infrastructure	• Technical, professional, medical and educational services (except religious services) were poorly developed • Gender based educational inequality • declining role of public delivery of health services, high OOP expenses on health • Cultural Heritage is not taken care of	• Progressively move to Direct Benefit Transfer (DBT) for all schemes of Government • Develop need based education services for the urban poor and other marginalized sections of urban society. • A GIS based heritage mapping should be done to conserve and promote the historical monuments located in cities
Housing and Affordability	• land is scarce in urban areas • Nearly 95% of housing shortage occurs for households in the EWS and LIG sections. • Promoting rental housing has escaped the attention of policy makers.	• A **national housing stock** must be created under the NUP Framework in collaboration with Mo/ Rural Development as envisaged under the PMAY (U) guidelines • In-situ upgrading that reduces the physical and legal vulnerability of self-built housing • **Inclusionary zoning** could also incorporate livelihood to create integrative, dynamic mixed-use spaces • Converting occupied public land into social rentals could be one way to expand rental housing.
Transportation and Mobility	• increased traffic congestion • different modes of public transport operate in silos and fragments • lack of designated space for road based public reduces its appeal to commuters who can afford other modes of transport	• Road 'improvement' projects should not occur at the expense of footpath space or cycle tracks. • A comprehensive **street vending policy** • All future airports, buses, trains and metro stations should be designed in a way to ensure seamless transits for commuters switching modes • Public bus operators should introduce **Intelligent Transport Systems (ITS)**

	• lack of a comprehensive parking policy	
Urban Finance	• economic and financial expertise is unavailable at the local level (especially in case of smaller municipalities) to assess at correct rates for services provided by the utilities. • poor paying capacity of a segment of population is used as an excuse for not charging even from others, who can and should pay.	• Insert a **'Local Bodies Finance List' (LBFL)** along the lines of the Union List and the State List. • Revenue Mobilization Plan to include property tax, professional tax, user charges, fees • ULBs who have been credit rated should implement **revenue enhancement plans** • There should be improved accounting system based on double entry and accrual system leading to better financial management and transparency.
Urban Governance	• Fragmentation of functions • Presence of parastatal bodies (for specific functions) has led to the proliferation of a multiplicity of agencies at the city level. • Most of the ULBs are understaffed	• Codify the roles of all functionaries • contemporary ways of accountability should be explored, such as recall and referendum • **Digitally enabled social audit** should be introduced. • outsourcing of functions and functionaries should bridge capacity gaps.
Urbanization and Information System	• lack of empirical data at town/ state/ national levels, lack of updated accurate base maps, lack of map data of underground infrastructure, outdated techniques of ground survey, use of citizens applications in silos	• Cities need to build **Integrated Command and Control Centre (ICCC)** • Through smart electricity grids and smart metering for electricity, water and gas, • ICT applications like Intelligent LED Street Lighting and Surveillance, networking of safety and security systems (CCTVs, police, traffic, etc.) • Implement **Open data Policies**
Environmental Sustainability	• India's cities are amongst the worst affected in terms of air pollution • The depletion in access to safe and usable surface and groundwater sources	• Plan and implement national and state level disaster plans. • Develop urban water management plans with a 5 to 10 year timeline. • Promote **extended producer responsibility (EPR)** principles in waste management rules.

10.2. SMART CITIES MISSION

Why in News?

The number of projects completed under the Smart Cities Mission has witnessed quantum jump of 182% in last one year.

Strategy of Smart Cities Mission

- The strategic components of Area-based development in the Smart Cities Mission are **city improvement (retrofitting), city renewal (redevelopment) and city extension (Greenfield development)** plus a Pan-city initiative in which Smart Solutions are applied covering larger parts of the city.
- The implementation of the Mission at the City level will be done by a Special Purpose Vehicle (SPV) created for the purpose.
- Every Smart City will have a Smart City Centre (SCC) (i.e. Integrated Command and Control Centre). The SCC functions as a city's nervous system where digital technologies are integrated with social, physical, and environmental aspects of the city, to enable centralised monitoring and decision making.

Background

- The Government of India launched the Smart Cities Mission (SCM) in 2015, to improve ease of living of citizens and create cities that are ahead of the curve in decisionmaking and problem solving.
- Although there is no universal definition of a Smart City, but broadly it can be described as an urban region that is highly advanced in terms of overall infrastructure, sustainable real estate, communications and market viability.

Achievements of the Mission

- **Completion of Projects**- The number of projects completed has seen a quantum jump of 182% over the last one year. The projects completed have jumped from 318 in June 2018 to 897 in June 2019.
- **Establishment of Smart City Centres (SCC)**- has already been done in 10 cities such as Ahmedabad, Vadodara, Surat, Pune, Nagpur etc. Various success stories have come up (refer the box).

- **Improvement in urban landscape**- Impact of SCCs is being felt, especially in five areas such as enhanced quality of services, safety and resilience, inclusiveness in city operations, faster emergency response management, and environmental sustainability.
- **Boost to the start-up industry**- it has provided a fillip to the entrepreneurial spirit of urban residents, thereby increasing employment.

Success Stories in Smart Cities Mission

- **Rajkot**- the crime rate has reduced by 18% over the past two quarters and there is an improvement in traffic challans issuance, indicating behavioural change. Monitoring of cleaning work through CCTV camera has led to reduction in instances of littering, urination in public, and nighttime burning of garbage.
- **Pune**- has installed flood sensors at key points around the city, which feed data to the SCC, enabling timely warning and response mechanism. Emergency callboxes have been installed at 120 locations to contact the nearest police station with just the press of a button.
- **Ahmedabad**- free Wi-Fi on BRTS corridors has increased ridership by 20,000 in March 2018, compared to Feb 2018.
- **Bhopal** has seen a rise in its property tax collections and is also able to track its transport services online.

Challenges in the Mission

- **Inadequate private participation**- At the outset, Smart City Mission had set a target of financing 21% of the total mission cost through private participation. So far, only 15% of the projects under implementation are under public-private partnership (PPP) mode.
- **Sources of funding are not clear**- While the top 60 cities have reported all their projects and the costs of most projects are stated in the project proposals (94%), but only 17 cities could identify the sources of finance at the level of each project.
- **Increasing inequality**- The mission has focused on the Area Based Development (ABD) model, where it indirectly incentivizes cities to focus the bulk of their funding on a small portion of the city. Thus, the ABD projects of 99 cities are found to be covering mere 7% of the total area and 80% of the total budget. Such approach creates inequality in and among cities.
- **Increasing focus on limited sectors of the Smart City**- such as 5 development categories of Transportation, Energy and Ecology, Water and Sanitation, Housing and Economy constitute almost 80% of the SCM budget. Other categories of IT, Governance, Culture and Heritage, and Health and Education constitute only 15% of the funding.
- **Recentralisation of Power**- There has been increasing role of the Special Purpose Vehicles (SPV) in the cities, which have encroached the functions of the Urban Local Bodies. Also there is lack of clarity about relationship and hierarchy between the SPV and the municipality.

Way Forward

- The efficacy of SCCs will improve with the integration of more and more services. The aim of the mission should be convergence with other city projects and breaking through the silos of various government departments.
- An enabling environment including governance frameworks, policy protocols, capacities of urban local bodies, and the nature of citizen-government engagement needs to be developed to further improve the urban space.

10.3. DRAFT NATIONAL LOGISTICS POLICY

Why in News?

Recently, Ministry of Commerce and Industry released Draft National Logistics Policy.

What is Logistics?

- It refers to overall process of how resources are handled and moved along the supply chain.
- It encompasses an array of activities beyond transportation, including warehousing, brokerage, express delivery, critical infrastructure services etc.

Significance of Logistics Sector

- **Employment**: Industry employs over 45 million people and is growing at the rate of 15% with sub-sector growing at even 30-40% per annum.
- **GDP**: India spends around 14.4% of its GDP on logistics and transportation. The sector is expected to grow at a CAGR of 15-20 percent between FY2016-2020.
- **Farmer Income:** an efficient logistic supply chain network has the potential to increase farmers' income manifold, which can **lead to a domino effect** on the overall economy.

Need of the policy

- **Fragmented Policy approach:** Different parts of the logistics value chain currently are being managed by multiple ministries and agencies which hampers coordinated oversight policy action.
- **High Logistics Cost:** Despite being recognised as critical driver of economic development, logistics cost in India is very high i.e. 13-14% of GDP as compared to USA 9-10%, Europe 10%, Japan 11%.
- **Skewed modal transportation mix** with 60% of freight moving on roads. It is significantly larger than in key developed economies.
- **Emerging new trends**- like domain expertise with specific skill set, environmentally friendly logistic and resilience to cyber threat demand an overhauling of man-power driven etc.

Government Initiatives for Logistic Sector

- Logistic sector has been **given infrastructure status** in 2017, which will ease-out fund related and other logistic bottlenecks.
- Government proposed **a Logistic Hub in Assam,** with the aid of Asian Development bank.
- Government has launched Logistic Ease Across Different States (LEADS) index in order to look at logistic bottleneck at state level.
- **Logistic Efficiency Enhancement programme** was launched to improve India's logistics efficiency.
- **GST** solves the problem of complex tax structure for logistics thereby leading to efficient decision making by logistic firms.

Highlights of Draft National Logistics Policy 2018

- **Policy Vision:** To drive economic growth and **trade competitiveness** through a truly integrated, reliable and **cost-effective** logistics network, leveraging **best in class technology**, processes and skilled manpower.

Policy objectives	Corresponding policy thrust areas
Creating a **single point of reference** of knowledge and information sharing platform for logistic.	• Creating a **National Logistics e-marketplace** as a one stop marketplace. • Setting up a **logistics data and analytics center** (LDAC)
Driving logistics cost as a % of GDP down to 10% and incentivize the sector to **become more efficient by promoting integrated development** of logistics	• Develop certain key corridors as **'Model Logistics' corridors** • Driving development of **Multi Modal Logistics Parks** (MMLP) to enable seamless and world-class multimodal freight transfer. • An **integrated policy and a Multi Modal Logistics Park Authority** should be established • Promoting cross regional **trade on e-commerce platforms** • Adoption of Warehouse Management System (WMS) and other IT-driven solutions
Improving India's ranking in the **Logistics Performance Index**	work on the **six indicators** of **World Banks' LPI** - Custom; International Shipment; Tracking & Tracing of trace consignment; Infrastructure; Logistic Competence; Timeliness of consignment
Reducing losses due to agri-wastage to less than 5% and thereby enhance agriculture price realization and farmer income.	Focus on providing **specialized nature of requirements** for packaging, transportation and storage of **perishable commodities**.
Encouraging adoption of **green logistics** in the country.	Policy visualises a reduction in **supply chain carbon foot print** through duty rationalization on alternative fuels, improved vehicle design etc. and also focus will be placed on the **3R – Reduce, Reuse and Recycle** in packaging.
Some Other Objectives and Thrust Areas	• Creating an **Integrated National Logistics Action Plan** • **Enacting a Framework Act on Integrated Logistics** • **Institutional Framework & Governance for Logistics** • **Doubling employment** in the logistics sector

10.4. REPORT ON PROJECT/ PROGRAM MANAGEMENT

Why in news?

A Task force under NITI Aayog has submitted a report on Project/Program Management, suggesting policy framework for project management for infrastructure projects in India.

Need of better project management practices

- Given the fact that each of the projects are unique, complex, involve multiple stakeholders, and require significant funds and time to complete, traditional ways of managing project have proven to be ineffective.

- **Poor project management** leads to –
  - Additional expenditure burden due to increased costs, which crowds out funding for more deserving projects.
  - Creating a culture of acceptance of delays and avoidable costs, which causes more cases to occur.
  - Economic burden due to delayed return in investments.
  - The increased cost of procurement due to monetization of higher risks perceived by contractors such as delay and scope creep associated with publicly funded projects.
- **Structured project management practices** would
  - maximize the limited resources and effectively respond to changing project requirements.
  - bring in skills such as project scoping, planning, scheduling, risk assessment, team building and quality control for getting complex projects completed with desired quality, on time and within budget.
  - bring in synergies, integration and a common language to all the complex program initiatives like Sagarmala, Bharatmala, Industrial Corridors, Smart Cities Mission, etc.

Major Recommendations

- **Develop a National Project / Program Management Policy Framework (NPMPF)**- considering the specific issues and requirements of the nation as a whole. It can refer to the already available global best standards on project/ program management, and suggest procedures and guidelines for effective project execution of public sector and PPP projects.
- **Establish separate Project/ Program Management delivery team**- which can be assigned to **audit the delivery issues** with mega projects and recommend, "fixes" to the existing projects.
- **Create a National Institute of Chartered Project Professional (NICPP)**- to become as the nodal institution to create a resource pool of competent project professionals. As per the report, Indian would need 70 lakh skilled project managers in the next 10 years.
- Share Holder Agreement (SHA) and State Support Agreement (SSA) should be included in the contract, to ensure proper Rehabilitation and Resettlement (R&R).
- Other important recommendations include
  - Introducing professional courses for institutionalizing project management.
  - Focus on preparing quality **Detailed Project Reports (DPRs)**.

11. TRANSPORT SECTOR

11.1. FIRST MULTI-MODAL TERMINAL ON INLAND WATERWAYS

Why in news?

India's first multi-modal terminal on inland waterways was inaugurated on by Prime Minister in Varanasi.

More on news

- This is the first of the multi-modal terminals being constructed on the National Waterway-1 as part of the World Bank-aided **Jal Marg Vikas project** of the Inland Waterways Authority of India.
- The project of multi-modal terminal and proposed Freight Village at Varanasi are expected to **generate 500 direct employment and more than 2000 indirect employment** opportunities.

Multimodal transport is carried out using different modes of transport such as roadways, railway, waterway, and airway.

Key benefits of multimodal transport are:

- **Minimizes time loss at trans-shipment points:** Multimodal transport operator maintains its communication links and coordinates that interchange onward carriage smoothly at transhipment points.
- **Provides faster transit of goods:** The markets are psychically reduced by faster transit of goods; the distance between origin or source materials and customers is getting insignificant.
- **Reduces the burden of documentation and formalities:** The burden of issuing multiple documentation and other formalities connected with each segment of the transport chain is reduced to a minimum.
- **Saves cost:** The savings in money resulting from these advantages are usually reflected in the through freight rates charged by the Multimodal transport operator (MTO) and also in cargo insurance cost.
- **Establishes only one agency to deal with:** The consignor/ consignee needs to deal with only the Multimodal transport operator in all matters relating to goods, or delay in delivery of goods at destination.
- **Reduces cost of exports:** The inherent advantages will help to reduce the cost of exports and improve their competitive position with pricing in the international market segment.
- **Less Congestion:** It helps to avoid over- burdening of any particular mode of transport and thus saves space and cost associated with congestion. Moreover, this would save fuel and lessen the pollution.

India has witnessed growth in Multimodal transport in the recent times and the sector is still evolving.

- The advent of containerization along with initiatives from the Government such as passing **Multimodal Transport Act, 1993** to the recent implementation of Goods and Services Tax have helped the country to progress towards an integrated transport system.
- Government is planning a Policy on Multi modal transportation.
- Economic Survey 2017-18 estimates that Indian Logistics sector which is worth around USD 160 billion is likely to touch USD 215 billion in the next two years with the implementation of GST. In order to realize this potential, the country will need to make effective use of its strengths in IT and look out for collaborations with experts in this field.

Potential of inland water transport (IWT) in the country: As per National Transport Policy Committee (NTPC) Report of 1980, the approximate length of navigable waterways in the country was 14,500 km.

- The National Waterways Act, 2016 declares a total of **111 National Waterways.** Out of this, 17,980 km of the river and 2,256 km of canals can be used by mechanized crafts.
- The **estimated cargo movement** on these waterways by the year 2022 is estimated to be **159 million tonnes** according to the report on Integrated National Waterways Transportation Grid submitted by RITES in 2014.

How does India compare with world in IWT?

- China, USA, European Union maintained and upgraded their river system on core routes that can support large modern vessel fleets up to 40,000 tons of cargo in single voyage.
- IWT in India has only 0.5% modal share; compared to 42% in Netherlands, China 8.7%; USA 8.3% and Europe 7%.
- China invested USD 15 billion in 2005-2010; Germany invested over 12 billion Euros in 2012 alone.

Challenges in developing National Waterways

- **Very low level of investment:** Lack of convergence between IWT and other modes of transport and more e**mphasis on development of rail and road networks** resulted in low level of expenditure on IWT.
- **High cost of development of Ancillary facilities:** Development of modern-day multimodal terminals, jetties, ferry points and river information systems is **highly capital intensive.**

- **Perception of IWT investment as high-risk investment:** This was a disincentive for the banks to advance loans to private players. It discouraged private participation also even through PPP mode.
- **Technical Challenges:** such as Development and maintenance of **Fairway width** of 2.5 m to 3.0 m depth, irregular **siltation**, **Speed Control regulations** to avert bank erosion and safety of other users, Safety against cross ferries, etc.

Benefits of inland waterways

- **Capital Savings:** The capacity augmentation of navigation on NW-1 through the Jal Marg Vikas Project estimated to entail a capital expenditure of Rs. 2.53 crore per km only. Compared to this road and rail each cost over 5 crore per km.
- **Savings in transportation costs:** IWT would have positive impact on the overall logistics cost. For e.g: 1 Horse Power energy moves 150 kg on road, 500 kg on rail and 4000 kg on water.
- **Environment friendly:** Use of modern inland water vessels, with natural gas (LNG/CNG) as fuel will reduce emission of SOx, NOx (70%), particulate matter (95%) and CO2 (25%). Hence will have negligible impact on ambient air quality. Other factors include-
    - It's a **non-water consumptive** transportation project with minimal resource depletion.
    - **Least fuel consumption per ton-km**, burden on road and rail transportation will come down resulting in less fuel consumption and consequent environmental pollution
    - **Negligible land requirement:** Due to minimum requirement of land acquisition (except in few places where terminals are likely to be constructed), there will be insignificant impact on ecology & biodiversity, agricultural activities as well as on the livelihood of the people.
    - Safe mode for hazardous and over-dimensional cargo
    - LNG/CNG engines have **lower noise level** than diesel engines, hence less impact on ambient noise level.
    - **Improved river flow** due to improvement / augmentation of navigation facilities will in turn benefit aquatic flora and fauna.
- **Supplementary mode:**
    - **Increase in economic opportunities** in the form of employment and business opportunities (both in relation to cargo movement and peripheral petty business activities).
    - **Access to local communities** in the form of a mode of transport to conduct activities on both sides of the river.
    - Better water flow through maintenance of minimum water levels will provide for **better fish production and catch**, which in turn will directly enable enhanced income for the fishing communities along the river stretch.
    - **Improved access to trading centres** and ancillary infrastructure (cargo handling, etc.) along the rivers and navigation will benefit local, regional and international business.

Initiatives to Develop Inland Waterways

- The **'Jal Marg Vikas Project'** on National Waterways-I (NW-I) in river Ganga, a large integrated IWT project, has been launched between Varanasi and Haldia covering a distance of 1380 kms at an estimated cost of `5369 crore.
- Based on techno economic studies, **eight new NWs have been taken up for development in 2017-18.** These include NW-16 (Barak river); NW 68 – Mandovi , NW 111 – Zuari; NW-37 (River Gandak) etc.
- In order to reduce the logistics cost of cargo and facilitate passenger movement between North East and mainland, **MOUs have been signed with Bangladesh**.
- To provide **institutional funding**, the Government has proposed to allocate 2.5 per cent of the proceeds of Central Road Fund for development and maintenance of National Waterways.
- **Integrated National Transportation Waterway Grid Study:** It was undertaken by IWAI through RITES with an aim to link first 6 National Waterways to National/ State Highways, Railways (wherever feasible) and Sea Ports (wherever feasible).

11.2. RAILWAY SAFETY

Why in news?

The Indian Railways made safety its foremost priority and achieved its best ever (in last 57 years) safety record in 2018-19.

More on news-

- Incident of **train collisions** has come down to **zero** in the year 2018-19.
- The incidents of **derailment** have decreased from 78 in 2016-17 to 46 in the year 2018-19.
- There has been an **81% drop** in the **number of deaths** from 152 in 2013-14 to 29 till January 31, 2019.
- All unmanned level crossings on broad gauge network have been eliminated.

General Reasons for Rail Accidents in India

Derailments constitute 50% of the total rail accidents, followed by 36% accidents at unmanned level crossings gates.

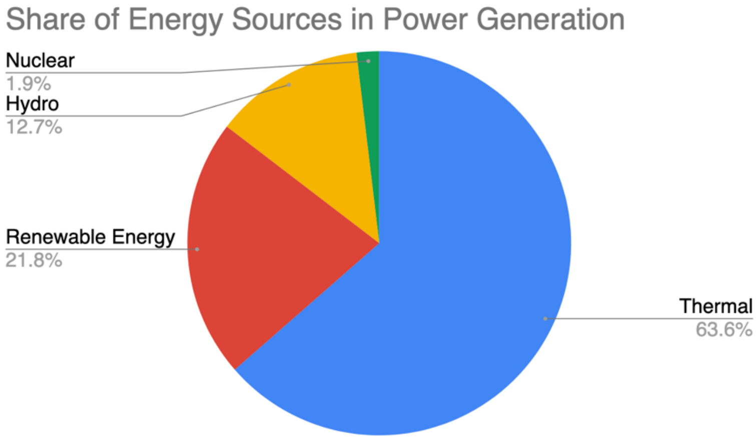
- **Lack of anti-collision technologies**
- **Staff deficit**
- **Inappropriate maintenance of tracks**
- **Resource crunch**
- **Poor Rolling stock (no LHB coaches)**
- **Negligence of the Government**

Steps taken by the Government

- **Strong acceleration in track renewal related works**- To eliminate track infirmities and to quickly replace old/damaged rail tracks, track renewal projects were prioritised. As a result, the speed of track renewal almost doubled from about 2,400 track km in 2014-15 to around 4400 track kms in 2017-18.
- **Modernisation of track and rolling stock monitoring and maintenance**- To ensure that defects in track or rolling stock are detected and addressed.
- **De-congesting railway network and upgrading rolling stock technology**- the government increased the average pace of commissioning new lines from an average of about 4.1 km per day (2009-14) to 6.5 km per day (2014-18). It is also upgrading the existing rolling stock by shifting to new technology such as LHB coaches and gradually procuring state-of-the-art diesel and electric locomotives.
- **Increased pace of elimination of unmanned level crossings**- which was close to 1,140 per year during 2009-14 was improved to about 3,400 unmanned level crossings in just 7 months (April 2018 – October 2018).
- **Ensuring adequate funds**- The **Rashtriya Rail Sanraksha Kosh** fund has been created for safety expenditure, which provides Indian Railways a dedicated corpus of `1 lakh crore for investing in safety projects during the 5 year period 2017 to 2022.
- **Other measures**- introduction of state-of-the-art signaling technology (European Train Control System (ETCS) level 2), proliferation of electronic interlocking, increased provision of foot over bridges, escalators, lifts in stations, filling safety related vacancies on priority.

12. ENERGY SECTOR

Introduction



- With multiple markets (coal, gas, oil, renewables, electricity, petrol and diesel) and infrastructure requirements for delivery to the final consumer (transmission and distribution grids, gas pipeline and petrol pumps), energy is one of the most complex sectors of the economy.
- The presence of scale economies in many sub-sectors, inter-connected nature of different sources of energy, different environmental implications of different fuels and social objective of access to energy at affordable prices greatly add to the complexity of policy making in this sector.

Priorities for India's Energy sector

- **To chart way to meet government recent announcements:**
    - Achieving universal electrification with 24x7 electricity by 2022. As of now, 304 million Indians live without access to electricity
    - Increasing share of manufacturing in our GDP from 16% currently to 25%
    - Target of Ministry of Petroleum to reduce oil imports by 10% from (2014-15 levels) by 2022.
    - Achieving INDC targets
- To **meet energy needs of vast population** predicted to go up to 1.6 billion by 2040.
    - 500 million people, still dependent on solid bio-mass for cooking
    - According to NITI AYOG exercise, the energy demand in India is likely to go up by 2.7-3.2 times between 2012 and 2040 and thus import demand could increase from 31% in 2012 to 36-55% in 2040.
- To increase coordination to achieve the goal of energy security as energy is handled by different Ministries with their own sectoral agenda
- To reduce cost due to air pollution – It is estimated to be 3% of its GDP and causes 1.2 million deaths every year.
- To set the new agenda consistent with the emerging developments in the energy world such as
    - **Changes in the global energy** mix where share of fossil fuel has reduced from 88% to 86% and share of renewable energy has increased from 12.5% to 14% during 2005-2015Ascendancy of gas vis-à-vis oil because of rising production of natural gas, lower prices than oil and 1/3rd lesser carbon emissions
    - **Over supply of oil and gas markets** have led to reduction in prices which has given fiscal space to countries like India to attempt larger energy policy reforms
    - **Reduction in price of renewable energy technologies** – Wind and solar prices have reduced by 60% and 52% respectively between 2010 and 2015
    - **Climate change concerns** – There is enhanced understanding of linkage between energy usage and poor environmental outcomes and awareness about air quality standards.

12.1. HYDRO POWER SECTOR

Why in news?

The Union government has approved various measures to promote hydropower sector.

Measures approved

- **Declaration of Large hydropower projects** (LHPs, i.e. >25
- MW) **as renewable energy projects.**
- **Hydro Purchase Obligation as a separate entity within Non-Solar Renewable Purchase Obligation for DISCOMS-** The HPO shall cover all LHPs commissioned after this order.

- **Tariff rationalization measures for bringing down hydropower tariff** such as providing flexibility to the developers to determine tariff by back loading of tariff after increasing project life to 40 years, increasing debt repayment period to 18 years and introducing escalating tariff of 2%.
- **Budgetary support for funding flood moderation component of hydropower projects**
- **Budgetary support to Cost of enabling infrastructure** i.e. roads and bridges.

Changes in India's Energy Mix after these measures		
Installed Capacity		
Renewable Sources	**Before including LHCs in RNE**	**After including LHCs in RNE**
in MW	75,055.92	1,20,455.14
In % share in energy mix	21.43	34.40
Share within Renewables (in %)		
Source	**Before including LHCs in RNE**	**After including LHCs in RNE**
Hydro	6.03	41.45
Wind	47.02	29.30
Bio-power	12.28	7.65
Solar	34.68	21.61

Efficacy of these measures

- Increase the share of renewable energy in the total energy mix of the country and will help India achieve target of 175 GW of renewable energy by 2022.
- As **renewable energy** is eligible for **priority sector lending** it would ensure easier availability of loans for large hydro power projects
- Hydro project**s** generate **employment** for local people in remote hilly and backward areas and **creates infrastructure** which lead to overall development of the area
- Storage based hydro power projects **improve the ground water recharge** and thereby improve the ground water level. It is understood that groundwater levels have significantly improved after the Indira Sagar Storage Project in Madhya Pradesh.

Issues faced by hydropower sector

- **Lack of enabling infrastructure**- such as roads, bridges to access remote areas where such potential sites are available.
- **Delay due to land acquisition**- for dam, power house etc.
- **Delay due to environment and forest clearances.**
- **Rehabilitation and Resettlement**-which invite opposition from locals for employment, extra compension etc. It also creates **law and order problems** like blasting, muck disposal.
- **Cultural/ Religious Issues**- sentiments attached with rivers
- **Political will**- lacks political traction due to long gestation period, Inter-state issues, especially over Riparian rights. E.g. Mullaperiyar Dam (between Kerala and Tamil Nadu)
- **High Tariff of Hydro Projects**- as compared to other sources of power (conventional as well as renewable sources) mainly due to construction of complex structures which have long gestation period, unavailability of loans of lower interest rate & longer tenures, high R&R cost, infrastructure etc.
- **Financing Issues**- High cost of Finance and lack of long tenure funding for hydropower projects.
- **Levying of water cess by the States**- e.g. J&K

Recommendations of Standing Committee on Energy for promotion of Hydro Power-

- **Expedite land acquisition** and **R&R (Resettlement and Rehabilitation)** process related to hydro power projects to **provide fair deal for the affected people as well as to fast track** the hydro power projects.
- **To integrate and fast track** the process of various clearances granted by the Ministry of Environment and Forest **to avoid time and cost overrun** in hydro power projects. Establishment of special cell to monitor and expedite the matters pending in the Supreme Court and National Green Tribunal (NGT).
- **Availability of long term loan at cheaper interest rate**- to ensure hydro power viability, since out of 16 stalled hydro power projects, 10 are stalled due to financial constraints**.**
- **Review the water cess imposed by the states**- as it further burden the already stressed sector. The Committee found that imposition of water cess is not fair considering the provision of

Hydro Energy Sector: Initiatives So Far

- **National Electricity Policy, 2005**: The policy lay emphasis on full development of the feasible hydro potential in the country.
- **Hydro Power Policy, 2008**: Under this transparent selection criteria to be followed by the States for awarding sites to private developers.
- **National Rehabilitation & Resettlement Policy, 2007:** It aims to minimize displacement and addressing special needs of Tribal and vulnerable sections who get displaced due to Developmental Projects.
- **Tariff Policy, 2016**: Policy aims to promote Hydro power generation including Private sector participation to provide adequate peaking reserves, reliable grid operation and integration of variable Renewable Energy sources.

12% of free power to the respective States from the hydropower projects.

- **Role of Central Public Sector Undertakings-** The present share of Private Sector in hydropower is only 7.5%. The State governments should **involve Central PSUs to enter** into **joint venture** with private sector to harness hydropower.
- **Creation of enabling infrastructure-** State Governments with the help of Central Government should take this responsibility needed for construction of hydropower projects. **Pradhan Mantri Gram Sadak Yojana** could be utilized by the states in this regard.

Way Forward

- For optimum utilization of India's hydro potential, there is a need for formulation of an enabling policy and taking this task on a mission mode with a timeline as it has already been done in case of development of solar and other renewable sources
- The cooperation and coordination between the Central and the State Governments is a pre-requisite.

12.2. REVIVAL OF STRESSED THERMAL POWER PLANTS

Why in News?

An empowered committee headed by cabinet secretary has suggested strong policy measures to revive stressed thermal power plants.

Background

- Following the Electricity Act which came into force in 2003 there were various developments that encouraged investment in the power sector, out pf which 45.48% was installed in private sector. This aggressive capacity addition has led to a widening gap in the overall demand and supply situation.
- However, an upsurge in demand has been observed, which is growing at more than 6 per cent per year. This is further expected to rise because of various government interventions like Saubhagya, Deendayal Upadhyaya Gram Jyoti Yojana (DDUGJY), Integrated Power Development Scheme (IPDS), Power for All, etc.
- Coal is the single largest source of energy for electricity production since 2, 21,803 MW is installed in thermal (including Coal + Lignite). There are various reasons that have been responsible for stress in some coal-based power plants to serve their debt.

Reasons for stress in Power Sector

The Committee identified following reasons for stress in the power sector-

- **Issues related to coal supply**- After the cancellation of 204 coal mines by the Supreme Court in 2014, many of the power projects became stranded without arrangements of adequate fuel supply. In addition, many projects were setup without firm coal linkages from Coal India Limited (CIL) leading to high cost of generation.
- **Slow growth in power demand**- Lower than anticipated growth in power demand coupled with a scenario of surplus supply has resulted in under-utilization of thermal power capacity. In addition to this low off-take/ difficulty in selling costlier power are also causing stress in thermal power projects.
- **Delayed payments by DISCOM's**- Delay in realization of receivables from DISCOMs impairs the ability of project developers to service debt in a timely manner and leads to exhaustion of working capital. In some cases, the DISCOM's have pressed for renegotiating terms of Power Purchase Agreement (PPA). This, coupled with non-payment of penalties / Late Payment Surcharges (LPS) is causing financial stress for such projects.
- **Inability of the promoter to infuse equity and service debt**- Many projects got delayed due to financial reasons and slow implementation by developers leading to project cost overruns.
- **Other Issues** include delay in disbursement / non-agreement amongst FIs, Delays in approval of working capital by lenders, Regulatory and contractual disputes, etc.

Recommendations of the Committee

- **Recommendations for Coal Allocation/Supply**
  - **Coal linkage for short term PPA**: Linkage coal may be allowed to be used against short term PPAs and power be sold through Discovery of Efficient Energy Price (DEEP) portal following a transparent bidding process.

- **Steps taken by Government to tackle stress in Power Sector**
  - Fuel linkages under **SHAKTI** (Scheme for harnessing & allocating koyla transparently in India).
  - Pilot **scheme for procurement** of 2500 MW power to address the problem of lack of Power Purchase Agreements (PPAs) in the country on competitive basis.
  - **Rationalization of Coal Escalation Index** which will largely take care of the issues of under recovery of the generator's dues.
  - **Additional cost implication to meet the new environment norms** shall be considered for being made pass through in tariff.
  - Allowing pass-through of any change in domestic duties, levies, cess, and taxes imposed by the government.
  - A new App **PRAAPTI** (Payment Ratification and Analysis in Power Procurement for Bringing Transparency in Invoicing of generators) has been launched to bring more transparency in the payment system by DISCOMs.
  - Other steps include **DISCOM reforms**, Coal linkage rationalization, etc.

  - **Termination of PPAs**: A generator should be able to terminate PPA in case of default in payment from the DISCOM with the facility to use linkage coal for short term PPAs for a period of maximum of 2 years or until they and another buyer of power under long/medium term PPA, whichever is earlier.
  - **Procurement by nodal agency**: A nodal agency may be designated which may invite bids for procurement of bulk power for medium term for 3 to 5 years in appropriate tranches, against pre-declared linkage by Coal India Limited (CIL).
  - **PSU as an aggregator of power**: National Thermal Power Corporation (NTPC) can act as an aggregator of power, i.e., procure power through transparent competitive bidding process from such stressed power plants and offer that power to the DISCOMs against PPAs of NTPC till such time as NTPC's own concerned plants/units are commissioned.
  - **E-auction of coal:** Ministry of Coal may earmark for power, at least 60 per cent of the e-auction coal, and this should be in addition to the regular coal requirement of the power sector.
  - **Linkages to be provided at notified prices without bidding**: The generator should be required to bid only once, for the procurement of PPA and linkage should be granted at notified price without any further bidding, to the extent of incremental coal production.
- **Recommendations to facilitate sale of power of the stressed power plants**- Old and high heat rate plants not complying with new environment norms may be considered for retirement in a phased and timebound manner at the same time avoiding any demand/supply mismatch.
- **Recommendations on Regulatory & DISCOM payment issues-**
  - Late Payment Surcharge be mandatorily paid in the event of delay in payment by the DISCOM.
  - PFIs providing the Bill Discounting facility may also be covered by TPA i.e. in case of default by the DISCOM, the RBI may recover the dues from the account of States and make payment to the PFIs.
- **Other recommendations:** PPAs, Fuel Supply Agreement and Long Term Open Access for transmission of power, EC/FC clearances, and all other approvals including water, be kept alive and not cancelled by the respective agencies even if the project is referred to NCLT or is acquired by any other entity.

12.3. DRAFT ELECTRICITY AMENDMENT BILL

Why in News?

Ministry of Power has sought comments on a revised draft of the Electricity Amendment Bill.

Background

- The three segments of the electricity sector in India (**generation, transmission, and distribution**) were initially bundled together with the state owned electricity boards. In the 90s, the generation segment was opened up to the private sector and later a few states restructured the system by segregating the three segments.
- The Electricity Act, 2003 was the next big reform attempt at the electricity sector regulation.
- However, **competition in the transmission and distribution segments has been limited** in India with very little participation from the private sector.
- The Electricity (Amendment) Bill, 2014 was introduced to: (i) increase competition in the sector by segregating the distribution segment into distribution and supply, (ii) rationalise tariff determination, and (iii) promote renewable energy.

Key Features of the Bill

- **Segregation of distribution network and retail supply of electricity**
- **Purchase and sale of power**: Power Purchase Agreements (PPAs) is a legal contract between the power plant (generation company) and the power distribution company (discoms). The amendments provide that all purchase or sale of power will be done through long/medium/short term PPAs.
- **Tariff ceiling by CERC/SERC**
- **Reforms w.r.t Subsidy Regime:**
    - **Move toward direct subsidy**
    - **Elimination of cross subsidy**
- **Renewable energy**:
    - **Renewable energy Definition** to include hydro (limit notified by the central government), wind, solar, bio-mass, bio-fuel, waste including municipal and solid waste, geo-thermal, tidal, co-generation from these sources, and other sources as notified by the central government.
    - **Renewable Purchase and Generation Obligation (RPO, RGO)**: The amendments define RPO and RGO which will be notified by the central government.
- **Provides for Smart grid and metering**

Benefits of the proposed amendments

- **Choice to consumers**: Separation between the infrastructure builder (for power distribution) and the licensee to supply would entail more than one electricity supplier in an area and consumer will have options of changing their power supplying company or utility based on the efficiency of their services.
- **End Sectoral Bias due to cross subsidy:** Differential pricing and subsequent cross subsidising raises the input costs for manufacturing and service sectors.
- **Breaking the cycle of subsidy and losses**: The DBT feature introduced has potential to eliminate losses incurred by the DISCOMS and is also beneficial to the end consumer as subsidy shall be directly transferred to the beneficiary.
- **24*7 Power supply:** The draft amendments propose that 24X7 power supply is an obligation and the state electricity regulatory commission can penalise the power distribution company (discoms), if it fails to do so.
- **Violation of PPA to be penalised**: This feature provides a major relief for power generators which lately have been facing brunt of states cancelling PPA citing high cost or lack of funds.
- **Boost for Renewable Sector:** The bill's features for renewable energy will help India to achieve its targets wr.t clean energy.

Issues with the Amendment

- **Ability of consumers to switch between suppliers:**
    - Consumers should have the facility to easily switch from one supply licensee to another and the supply of power to the consumer should not be interrupted during such transition. The amendments do not explicitly provide for how such switching will work, and **what will happen during the transition from one supplier to the other**.
    - The 2003 Act provides for multiple licensees to set up their own distribution network in the same area, thus allowing for competition. However, the electricity distribution segment has not seen much competition. Setting up a new network requires **significant capital investment** and hence acts as an entry barrier for new participants.
- **Procurement exclusively via PPA:** Supply companies may face unanticipated demand at times and thus the question is why they are not allowed to procure any power through ways other than PPAs.
- **Composition of Selection Committee for SERCs:** The proposed SERC selection committee has only one representative from the state, and five from the centre. Additionally, the rationale for having a serving judge of the Supreme Court on the selection committee of all SERCs in the country is unclear.
- **Issues with removing cross subsidies may increase subsidy burden on exchequer**:
    - **Increased tariffs for low paying consumer:** It could increase the tariffs for the currently low paying consumers (agricultural and residential) who are being subsidised.
    - **Subsidy burden on the exchequer**: The state or central government may choose to alleviate any increase in their tariffs by giving them explicit subsidies through DBT. This could increase the subsidy burden on the exchequer

12.4. PRADHAN MANTRI UJJWALA YOJANA (PMUY)

Why in News?

Recently, government has extended the scope of beneficiaries to be covered under Pradhan Mantri Ujjwala Yojana (PMUY).

About the move

- Earlier, **beneficiaries** under the PMUY included **all the BPL families** who suffer with at least **one deprivation** under **Socio-economic caste census 2011.**
- It has been expanded to cover all **SC/ST** households, beneficiaries of Antyoday Anna Yojana (**AAY), PMAY (Gramin), forest dwellers, most backward classes (MBC), Tea and Ex-Tea Garden Tribes, people residing in Islands or rivers island.**
- Now, the scheme will cover **all the poor households** of the country. Under this, new beneficiaries will be those among holders of both ration cards and Aadhaar, who will identify themselves as **poor through self-declaration.**

Achievement of PMUY

- LPG penetration in India has risen from 56% in 2014 to 89% in Dec 2018.
- Till Dec 18, of the 5.8 crore connection released, 3.8 crore are beneficiaries from the SECC list and 2 crore from the other seven categories added later.

About the PMUY

- **It aims** to provide **8 crore deposit free LPG connections** to women from BPL households by 2020.
- The LPG Connection is released **in the name of adult woman of the BPL Family**, with a financial support of RS 1600/- subject to the condition that **no LPG connection exists** in the name of any family member of the household.
- Consumers will have the option to purchase **gas stove and refills on EMI** (zero interest), recovered through LPG subsidy received by the beneficiary.

Expected outcomes of PMUY

- It was launched to make clean energy affordable and accessible because **air-pollution** in rural households becomes lethal due to use of wood or cow dung as cooking fuel.
- It would lead to savings in cost and time spent in collecting wood, resulting thereby in improved opportunities to earn income and spend time with the family.
- It would have a positive outcome on health, especially that of women, children's education and employment.

Challenges in further adoption

- **Overall Cost:** Most of the states cited **initial high cost** as a major barrier for adoption of this scheme. Similarly, non-support by the government at the **refilling stage** forces the poor to pay more than rich in urban areas.
- **Long waiting time and sparse LPG distribution centres:** The number of distributors has not kept pace with the increasing number of active LPG consumers e.g. between 2016-2018, the total number of active LPG consumers increased by 31 per cent, while total number of distributors went up by 9 per cent.
- **Information Gap:** Data on PMUY connection is provided only at the state level and district-wise disaggregation is not available. Therefore, it is difficult to conclude that households are moving away from using solid fuels for cooking. They are possibly being used for other purposes.

What needs to be done?

- **Demand-side intervention:** There is a need for more information about the scheme in the public domain for a comprehensive evaluation and mid-course correction. For this, village-level **ASHA workers** can be roped in to create awareness about the ill-effects of **traditional chulhas,** which will create a **bottom-up demand** for cleaner fuels.
- **Strengthening the supply chain:** By ensuring adequate provisions for affordability, availability, and accountability of the scheme.
- **Diversified Options**: Government should try to diversify fuel options and **make cylinders in different portable sizes** and make **door-to-door refilling service available**, in order to reduce leakages and pilferages.

12.5. DISCOM DEBT TO RETURN TO PRE-UDAY LEVELS

Why in news?

As per a recent report of the rating agency CRISIL, the total debt of state-owned DISCOMS is set to **increase to pre-Uday levels of Rs 2.6 trillion** by the end of this fiscal year.

About Ujwal Discom Assurance Yojana (UDAY)

- In 2015, The Ministry of Power, Government of India launched this scheme, to improve the **financial health and operational efficiency** of India's debt-ridden power distribution companies (DISCOMS that supply power to consumer. They can be a private or a government company.
- It involved a tripartite agreement (Memorandum of Understanding, MoU) between Ministry of Power (MoP), state governments and respective DISCOMs.
- Under UDAY, DISCOMS can convert their debt into state government bonds, but are required to fulfill certain conditions such as **AT&C loss reduction, mandatory metering, power purchase planning and performance monitoring.** In lieu, state governments took over three-fourths of discom debts, thus reducing the interest burden.
- After UDAY had been implemented, aggregate discom debt had fallen from ₹ 2.7 lakh crore in September 2015 to ₹ 1.9 lakh crore in FY16 and ₹ 1.5 lakh crore in FY17.
- A CRISIL report has analyzed the DISCOMS in 15 states that account for 85% of the aggregate losses. As per it, the downward trajectory is now expected to reverse, moving up to ₹ 2.28 lakh crore in FY19 and ₹ 2.64 lakh crore in FY20.

Features of UDAY Scheme

State Takeover of Discom Debt	Debt takeover mechanism	UDAY Bonds	Treatment of residual debt	Future Discom financing
Scheme available only for State Discoms including combined generation, transmission and distribution undertakings	Debt of Discom will be taken over in the priority of debt already due, followed by debt with highest cost.1	Non-SLR bonds issued by States shall have maturity period of 10-15 years with a moratorium on repayment of principal up to 5 years, as required by the State	Up to 25% of the grant can be given as equity where the Discom requires equity support.	Bank/FIs henceforth cannot advance short term debt to Discoms for financing losses.
States shall take over 75% of Discom debt as on September 30, 2015. Debt shall be taken over as: 2015-16 - 75% 2016-17 - 25%	Transfer to Discom by State will be as grant with an option to spread the grant over three years (MoP can further relax by 2 years for high debt States)	10 year Bond Pricing: The 10 year UDAY bonds would be priced at the 10 year G-sec + 0.50% spread of 10 year SDLs + 0.25% spread for non-SLR status on semi-annual compounding basis, or market determined rate whichever is lower. This may be further reduced if the interest is paid on monthly basis.	Discom debt to be taken over by the State will include Discom bonds which are committed to be taken over by the State as part of FRP 2012 including bonds already taken over in 2015-16	Working capital loans from Bank/FIs will only be allowed up to 25% of the Discom's previous year's annual revenue.
Discom debt is de facto borrowing of State which is not counted in de Jure borrowing. Principal debt taken over will not be included in fiscal deficit of States. However, interest has to be serviced within FRBM limits.	State will issue non SLR including SDL bonds in the market or directly to the respective banks/ Financial Institutions (Fis) holding the Discom debt to the appropriate extent. Proceeds shall immediately be transferred by the States to the Discom, which in turn shall discharge the corresponding amounts fo Bank/FIs debt.	Bonds to be issued against the loans of FIs, including REC and PFC, would first be offered for subscription by the market including pension and insurance companies. Balance, If any, would be taken over by banks in proportion to their current lending to Discons.	For amount transferred as loan, the interest rate payable by the Discoms to the State for the intervening period shall not exceed the rate of interest on the bonds issued by the State.	States shall take over the future losses of Discoms in a graded manner FY16 - 0% of the loss of FY15 FY17 - 0% of the loss of FY16 FY18 - 5% of the loss of FY17 FY19 - 10% of the loss of FY18 FY20 - 25% of the loss of FY19 FY21 - 50% of the loss of FY20

Reasons for increase in debt levels of states

- **Limited Fiscal space**- it makes continuous financial support to their DISCOMS difficult. In 2016, most states had the fiscal headroom to assume three-fourths of the debt of their discoms, but now, because of the deterioration in their finances over the past few years, the space has become limited.
- **Operational Inefficiencies**- e.g. across several states, there is a lack of effective billing procedures, poor measurement of power consumption, and ineffective monitoring of power theft.

- **Increased Power Purchase Cost-** After the one-time measures under UDAY, the power purchase costs have now increased by 5 per cent in the first nine months of 2018-19. Further the input costs of coal and freight have gone up.
- **Lack of structural reforms-** such as AT&C losses reduced by only 400 bps by December 2018 from pre-UDAY levels, against the target of reducing AT&C losses by 900 basis points to about 15% in 2018-19.
- **Lack of adequate tariff hikes-** The average tariff increases were a paltry 3% per annum against the target of implementing regular tariff hikes of 5-6% per annum and now with the focus on new rural connections, further increases are unlikely. Even if the Discoms have improved their operational efficiency, but state regulators in some cases have not allowed electricity tariffs to keep pace with input costs.

Steps which need to be taken

- **Power banking:** DISCOMs could also resort to power banking arrangements wherein the state could smoothen the seasonal variations by supplying energy during surplus situations (e.g. in the month of June/July for Karnataka) to other states, which experience deficit situation during these months.
- **Separate power planning cell in DISCOMs:** This cell could support the demand forecasting exercise and coordinate with other state nodal agencies.
- Need to ensure **cost-reflective tariffs** so as to maintain the financial health of DISCOMs.
- Material **reduction in AT&C losses** using measures such as smart metering, installation of prepaid meters on government buildings.
- **Streamlining the energy auditing process**: In order to have a successful outcome from the smart metering initiative, all Distribution Transformers should be installed with smart meters, which could record real-time data remotely.

Conclusion

Till now, the focus was at the intervention in terms of reducing the debt burden. But, in future the focus needs to be at interventions in terms of technology and enablement to further achieve the same objectives. This will require aerial bunch cables, smart metering, providing some funds for dedicated police units which will be attached with the distribution companies, to prevent theft etc.

13. MISCELLANEOUS

13.1. NOBEL PRIZE IN ECONOMICS

Why in news?

American economists William Nordhaus and Paul Romer have been awarded the Nobel Prize for their work on understanding how economies can grow sustainably, by integrating innovation and climate with economic growth.

1987 Nobel Prize winner Robert M Solowwas among the first to identify technological progress as the key determinant of growth in the long run.

However, for Solow, technological innovation was "exogenous" to his model.

What is unique about this year's Nobel Prize winners?

This year's Nobel Prizes have been awarded to Economic theories with direct political and practical implications. Both the Laureates life work goes against the traditional model of growth and development. e.g. Growth model of Nobel Laureate Robert Solow which provides a relationship between growth of workforce and capital with long term economic growth.

Nobel Winners' Work

William Nordhaus

- Nordhaus believes that climate change can be addressed by ensuring correct pricing of polluting resources like fuel through government interventions e.g. higher taxes on petrol, diesel.
- His models that integrated population growth, fossil fuel use, income growth, and global warming became the basis for most calculations of the costs and benefits of various anti-global warming interventions.
- First person to create an "integrated assessment model", a quantitative model that describes the interplay between economy and climate.
- Putting a price on carbon is the main tool for alleviating climate change.

Paul Romer

- Technological innovation and skilling of workforce are the real sources of sustainable growth.
- Proposes the "endogenous growth model" where technological progress is seen as the outgrowth of businesses and other entities investing in research and development.
- A market led economy may undersupply technological innovations
- He recommended the use of subsidies, patents and other forms of government intervention to encourage economic growth through increased investment in technology.