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JAPAN INTERNATIONAL COOPERATION AGENCY (JICA)

MINISTRY OF INDUSTRY, INDIA

INDIA

THE MASTER PLAN STUDY ON THE INDUSTRIAL MODEL TOWN

FINAL REPORT

DECEMBER 1993

YACHIYO ENGINEERING CO., LTD.

in Association with

TECHNO CONSULTANTS, INC.

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Preface

In response to a request from the Government of India, the Government of Japan decided to conduct the Master Plan Study on the Industrial Model Town in India and entrusted the study to the Japan International Cooperation Agency (JICA).

JICA sent to India a study team headed by Mr.Hisashi Kurokouchi, Yachiyo Engineering Co.,LTD., four times between November 1992 and July 1993.

The team held discussions with the officials concerned of the Government of India, and conducted field surveys at the study area. After the team returned to Japan, further studies were made and the present report was prepared.

I hope that this report will contribute to the promotion of the project and to the enhancement of friendly relations between our two countries.

I wish to express my sincere appreciation to the officials concerned of the Government of India for their close cooperation extended to the team.

December 1993

Kensuke Yanagiya

Kensuke Yanagiya
President
Japan International Cooperation Agency

FINAL REPORT

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Abbreviation

BBMB	:	Bhakhra-Beas Management Board
BIFR	:	Board of Industrial and Financial Reconstruction
BUDA	:	Bangarole Urban Development Authority
BWSSB	:	Bangalore Water Supply and Sewerage Board
CAD	:	Current Account Deficit
CCS	:	Cash Compensatory Support
CDOT	:	Central Department of Telecommunication
CII	:	Confederation of Indian Industry
CPCB	:	Central Pollution Control Board
CPHEEO	:	Central Public Health Environmental Engineering Organisation
CTCP	:	Chief Town and Country Planner
CWSS	:	Cauvery Water Supply Scheme
DI	:	Directorate of Industries
DID	:	Department of Industrial Development
DMA	:	Delhi Metropolitan Area
DOE	:	Department of Electronic
DSIDC	:	Delhi State Industrial Development
DTA	:	Domestic Tariff Area
EIS	:	Environment Impact Statement
EOU	:	Export Oriented Unit
EPCG	:	Export Promotion Capital Goods
EPZs	:	Export Processing Zones
FERA	:	Foreign Exchange Regulations Act
FIPB	:	Foreign Investment Promotion Board
GDE	:	Gross Domestic Expenditure
GDP	:	Gross Domestic Production
GVA	:	Gross Value Added at Factor Cost
HSEB	:	Haryana State Electricity Board
HSIDC	:	Haryana State Industrial Development Corporation
HSPCB	:	Haryana State Pollution Control Board
HUDA	:	Haryana Urban Development Authority
IAG	:	Industrial Assistance Group
I & C	:	Industries & Commerce
IDBI	:	Industrial Development Bank of India
IDC	:	Interest During Construction
IDR	:	Industries' Development and Regulation Act 1951

IETF	:	Indian Engineering Trade Fair
IFCI	:	Industrial Finance Corporation of India
IIC	:	Indian Investment Center
IMT	:	Industrial Model Town
JICA	:	Japan International Cooperation Agency
KEB	:	Karnataka Electricity Board
KEONICS	:	Karnataka State Electronic Development Corporation Limited
KHDO	:	Karnataka Housing and Development Department
KIADB	:	Karnataka Industrial Areas Development Board
KSFC	:	Karnataka State Financial Corporation
KSIIDC	:	Karnataka State Industrial Investment and Development Corporation Limited
KSIMC	:	Karnataka Small Industries Marketing Corporation Limited
KSPCB	:	Karnataka State Pollution Control Board
KSSIDC	:	Karnataka State Small Industries Development Corporation
KPC	:	Karnataka Power Corporation Limited
KUM	:	Karnataka Udyog Mitra
KUWSDB	:	Karnataka Urban Water Supply and Drainage Board
L/I	:	Letter of Intent
LUT	:	Legal Undertaking
MAPP	:	Madras Atomic Power Plant
MRTP	:	Monopolies and Restrictive Trade Practices Act, 1969
MUSS	:	Master Unit Substation
NCR	:	National Capital Region
NEXIM 91	:	The Exim Policy 1991
NFE	:	Net Foreign Exchange Earnings
NH	:	National Highway
NIP 91	:	New Industrial Policy
NLC	:	Neyveli Lignite Corporation
NOIDA	:	The New Okhla Industrial Development Authority
NRI	:	Non Resident Indian
NTPC	:	National Thermal Power Corporation Ltd.
PAB	:	Project Approval Board
PICUP	:	The Pradeshiya Industrial & Investment Corp. of U.P.
PMP	:	Phased Manufacturing Programmes
PWD	:	Public Works Department
RABMN	:	Remote Area Business Message Network
RBI	:	Reserve Bank of India

REP	:	Replenishment
RLU	:	Remote Line Unit
Rs	:	Rupee
SDF	:	Standard Design Factory
SDP	:	State Domestic Product
SEB	:	Special Empowered Board
SFC	:	State Financial Corporation
SIA	:	Secretariat For Industrial Approval
SPA	:	School of Planning and Agriculture
SSI	:	Small-Scale Industry
SWA	:	Single Window Agency
TECSOK	:	Technical Consultancy Service Organisation of Karnataka
UPFC	:	The Uttar Pradesh Finance Corp.
UPPCB	:	Uttar Pradesh Pollution Control Board
UPSEB	:	The Uttar Pradesh State Electricity Board
UPSIDC	:	U.P. State Industrial Development Corp.

Unit and Measure

Crore	:	10 Million Rupee
Lakh	:	0.1 Million Rupee
KLD	:	Kilolitre per day
MLD	:	Million Litre per day

Currency

Rupee	:	Rs. 30.5 = 1 US Dollar

CHAPTER 1 OBJECTIVES OF THE STUDY AND SCOPE OF WORK

CHAPTER 1 OBJECTIVES OF THE STUDY AND SCOPE OF WORK

1.1 Scope of Work

India's Ministry of Industry and Department of Industrial Development (DID) and the Japan International Cooperation Agency (JICA) agreed upon the Scope of Work (S/W) for this study on August 7, 1992.

1.2 Objectives of Study

The research efforts sufficiently demonstrate that the primary issue is to introduce foreign capital, investors, and technology transfers to India. Further, it was observed that the combination of "Soft" and "Hard" factors can provide the country effective tools for moving closer to large-scale economic reinvigoration, increase domestic industries' production capabilities, and enhance international competitiveness in the world markets.

According to the S/W, the objectives of the study are:

(1) to present appropriate recommendations for further promotion of multinational foreign investment, including technology transfers;

(2) (a) to make recommendations of appropriate candidate site(s) for formulation of an Industrial Model Town (IMT) in four candidate sites at Bangalore (Bidadi and Sathnur) and Delhi (NOIDA and Gurgaon) refer to Fig. 1-2; and

(b) to formulate the IMT conceptual plan for the site(s) recommended and mutually agreed upon by the Study Team and representatives of authorised departments and agencies of the Indian Government.

1.3 Methodology

The study and research was accomplished in the following manner according to "Fig. 1-1 Study Implementation Flowchart".

(1) Preparatory Work in Japan: Mid October - Mid November 1992

- Collection and Analysis of the Existing Data
- Collection of the Relevant Information
- Preparation of Questionnaires

- Preparation of Implementation Programme for Investment Demand Survey
- Preparation and Submission of the Inception Report

(2) Field Survey in India (1st Stage): 23rd November - 6th December 1992

- Presentation of, and Discussion on the Inception Report
- Discussion with relevant organisations
- Field study on the canadidate sites
- Local investment demand survey

(3) Work in Japan (1st Stage): Beg. of December 1992 - End of January 1993

- Review of the Background of the Study
    - Trends in Indian Economy
    - Structure of Industrial Sector
    - Production and Trade in the Industrial Sub-Sectors
    - Investment Climate and Foreign Investment
    - Existing EPZs and Industrial Estates
- Present Policy Environment
    - National Development Policy
    - Industrial Development Policy
    - Finance and Banking System Policy
    - Tariff and Trade Policy
    - Industrial Location and Regional Development Policy
    - Human Resources Development Policy
- Collection of the Relevant Information
- Foreign Investment Demand Survey

    An investment demand survey was commenced for Japan, the United States, and Germany.
- Preparation of Schedule for Field Survey (2nd Stage)

(4) Field Survey in India (2nd Stage): 31st January - 28th March 1993

- Investment Climate Survey
    - New industrial policy
    - Relevant laws and regulations in investment promotion
- Interview Survey with Foreign Investors, Joint Ventures and Domestic Enterprises
    - Technology transfer
    - Creation of employment opportunities

_ Development of linkage/supporting industries
_ Systems and functions of investment promotion

•Supplementary Study to Interview with Relevant Organisations

•Field Study on the Present Conditions in and around the Candidate Sites, namely, Bangalore (Bidadi and Sathnur),and Delhi (NOIDA and Gurgaon).

_ Topography and land use
_ Infrastructure (water supply, electricity, telecommunications, transportation, waste water and sewage treatment, industrial solid waste)
_ Accessibility
_ Supporting Industries
_ Labour Force
_ Training/Education/Research Facilities
_ Housing Conditions
_ Medical and Public Health Hygiene Facilities
_ Urban Amenities
_ Social and Environmental Situations

•Preparation of Progress Report (I)

•Presentation of, and Discussion on Progress Report (I)

(5) Work in Japan (2nd Stage): Beg. of May - End of June 1993

•Analysis of the Result of the Field Survey (2nd Stage) and Investment Demand Survey

_ Requirements/conditions from the investors' point of view
_ Comparison with the investment environment in neighboring countries highlighting the specific advantages of India
_ Analysis of potential foreign investors to India

•Collection of the Relevant Information

•Recommendations

_ Policies and Incentives for Attracting Foreign Investment to the IMT
_ Systems and Functions for Promotion of the IMT

•Formulation of Basic Concept of the IMT in India

_ Prerequisites for the IMT with respect to infrastructure and management
_ Comparison of Candidate Sites

•Preparation of Interim Report

(6) Field Survey in India (3rd Stage): 4th July - 31st July 1993

- Investment climate supplemental survey
- Site selection: recommendations
- Field survey on the selected site
- Preparation of Progress Report (II)

(7) Work in Japan (3rd Stage): Beg. August - Beg. of October 1993

- Analysis of the Results of the Field Survey (3rd Stage)
- Collection of Relevant Information
- Conceptual Design of the IMT
- Preparation of Draft Final Report

1.4 Report Compilation

This report is a compilation of three broad investigative research categories up to the time of publication. For example, Chapter 6, IMT Concepts, was formulated based on Chapters 1 to 5, which refer explicitly to the present conditions and subjects that should be improved regarding structural conditions in India. A second category, Chapters 7 to 10, best describes the refining of earlier guiding precepts found in the comparative analyses between the four candidate site locations. The remaining chapters represent the culmination of prior efforts and will provide the fundamental recommendations regarding policies, schemes, and the planning for the execution of the IMT.

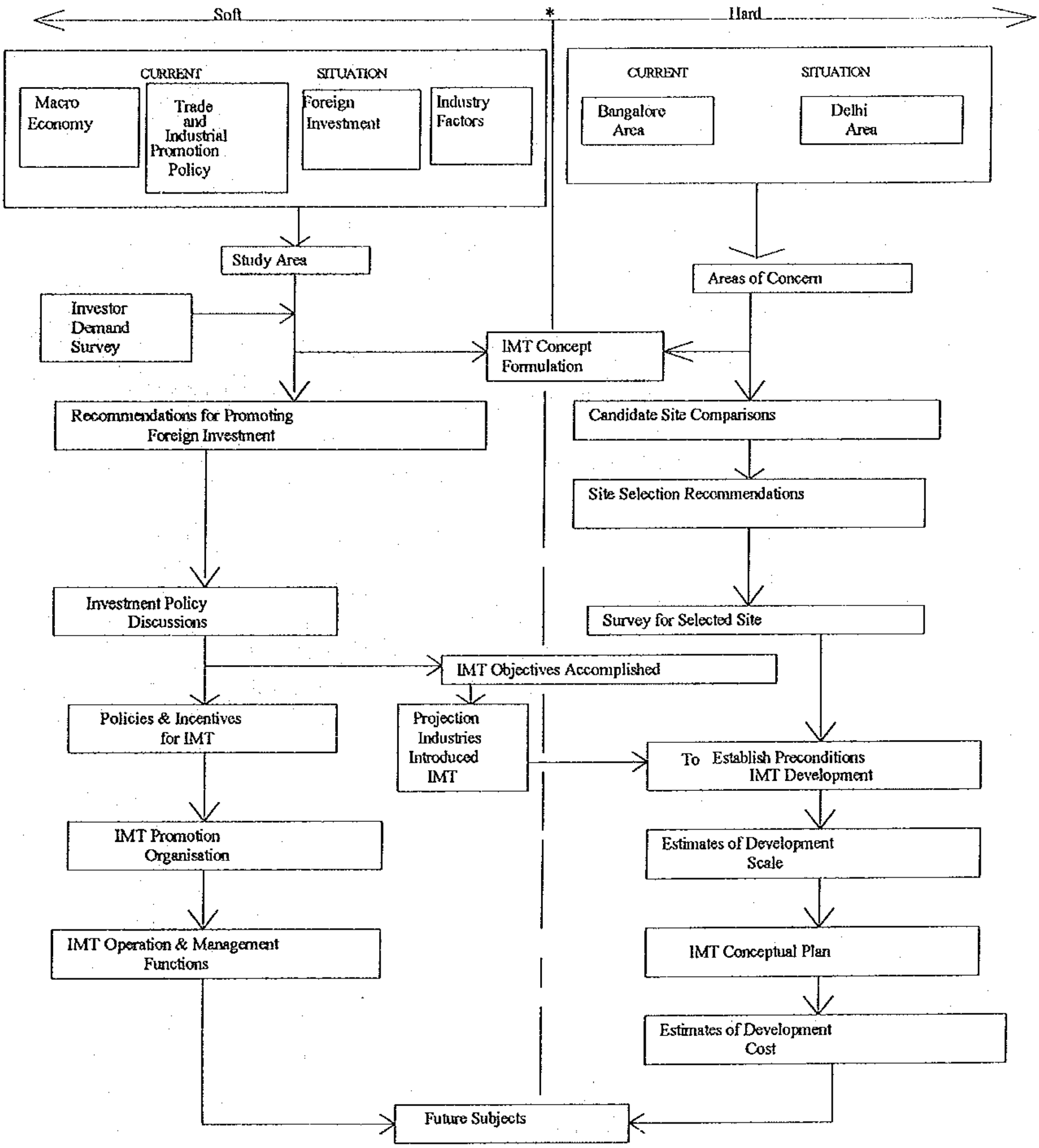


Figure 1-1 Study Implementation Flowchart

THE MASTER PLAN STUDY ON THE INDUSTRIAL MODEL TOWN	
National Map of INDIA	No. Fig. 1-2
0 500km 1,000km	
JAPAN INTERNATIONAL COOPERATION AGENCY	

CHAPTER 2 MACRO ECONOMY OF INDIA

CHAPTER 2 MACRO ECONOMY OF INDIA

2.1 Annual Records and Trends

In order to study the time-bound trends of imports, domestic production, domestic consumption, and exports, and the association relations of these factors, Table 2-1 is provided.

The items marked I, II, and III are based on the original commodity classifications given in the "Economic Survey" 1991-92, and 1992-93, 7.2 and 7.3, and were rearranged for strategic analysis. The categories are as follows:

Category I: Primary products - agricultural and allied products, forestry and marine products, ores and minerals, coal and petroleum oil.

Category II: Manufactured goods - intermediate and finished goods, except capital goods.

Category III: Capital goods - machinery and transport equipment, including electronic goods.

2.1.1 Import Trends

(1) Composition of Imports

The component ratio for the structure of three categories of imported goods is shown in Table 2-2 (note: the data is derived from Table 2-1).

Table 2-2 Composition of Goods Imported (%)

Year	I	(Petroleum Oil)	(Non-Oil)	II	III
1980	46.4	(41.6)	(4.8)	35.2	14.4
1985	31.6	(25.0)	(16.6)	44.9	20.9
1986	18.9	(13.9)	(5.0)	49.7	31.3
1987	24.3	(18.0)	(6.3)	45.4	28.8
1988	22.3	(15.2)	(7.1)	53.5	23.7
1989	21.4	(17.5)	(3.9)	54.2	24.0
1990	27.7	(25.0)	(2.7)	47.9	23.3
1991	29.9	(27.4)	(2.5)	48.7	21.1

Table 2-1 Marco Economic Data

(Unit: Rs. billion for Factors 1 to 6)

Factors	*1. Imports (CIF) [2]*				*2. Domestic Production [1]*				*3. Gross Domestic Expenditure [2]*		*4. Export (FOB) [2]*				*5. Trade Balance*	*6. GDP [3]*	*7. GDP Growth Rate [3]*	*8. Population (million*	*9. Per Capital GDP Rs. [3]*	*10. Exchange Rate per US$1.00*	*11. Foreign Exchange Reserves US$ (million)*
Items Year (F.Y.)	I	II	III	Total	I	II	III	Total	Pvt. Final Consm.	Gross Fix Cap. Formation	I	II	III	Total							
1980	58 (52) [4]	44	18	125	504	145	51	700	981	262	25	32	6	67	-58	1224	7.2	685	1786	7.908	5850
1985	62 (49)	88	41	196 (137)	595	203	72	870	1185	365	44	56	9	108 (76)	-87	1565	4.1	763	2051	12.253	5972
1986	38 (28)	100	63	201 (134)	591	217	77	885	1411	387	45	69	9	124 (83)	-76	1632	4.3	779	2094	12.778	5924
1987	54 (40)	101	64	222 (128)	596	233	82	911	1294	412	49	96	11	156 (90)	-65	1703	4.3	795	2142	12.966	5618
1988	63 (43)	151	67	282 (162)	690	252	89	1031	1400	448	52	134	15	202 (116)	-80	1889	10.9	811	2329	14.482	4226
1989	76 (62)	192	85	354 (212)	706	270	96	1072	1412	486	63	182	24	276 (165)	-77	1995	5.6	827	2412	16.649	3368
1990	120 (108)	207	101	432 (199)	740	290	103	1133	N/A	535	87	209	28	325 (150)	-106	2097	5.2	846	2478	17.943	2236
1991	143 (131)	233	101	478 (192)	733	289	102	1124	1641	591	113	286	41	440 (178)	-38	2123	1.2	860	2468	24.474	5631

Note:
[1] Amounts are quoted at 1980-81 prices
[2] Amount quoted in current market prices.
[3] At factor cost, at 1980-81 prices.
[4] The figures in brackets show the amount of petroleum oil and lubricants imports.

Category I: Primary Product
Category II: Manufactured Goods
Category III: Capital Goods

Total ( ): Constant Price at 1980-81

Sources:

Factor 1) & 4) "Economic Survey" 1992-93, 7.1 (A) S-84
Factor 2) Same as above 1-3, S-5, Rearranged
Factor 3) United Nations, "Statistical Yearbook for Asia and the Pacific 1991: 1991 "Eighth Five Year Plan" Table 3.2 adjusted to 1980 prices level.
Factor 5) "Economic Survey" 1992-93 7.1 (A), S-84
Factor 6) Same as above 1-3, S-5
Factor 7) Same as above 1.6, S-10
Factor 8) Same as above 0.1, S-1
Factor 9) Calculated 6)/8)
Factor 10) "Economic Survey" 1992-93, 6.5, S-83
Factor 11) Same as above 6.1, S-74

(2) India's import structure characteristics indicate that "petroleum oils and lubricants" have a very large share of India's imports, averaging 20 per cent for the last seven years; for 1990 and 1991, import shares were 25 and 27 per cent, respectively. And fluctuations in oil prices have influenced total import amounts.

The long term trends examined from 1980 to 1991, indicate the following for each category of goods.

Category I: Although the total amount substantially fluctuates year to year due to oil price fluctuations, a general downward trend was observed.

Category II: A constant upward trend, with a relatively large share; to about 50 per cent.

Category III: Although the component ratio remains small (approx. 25 per cent average for the last seven years), a steady upward trend can be observed.

(3) For reference, the component ratio of Category III goods imports (capital goods) is compared with other countries (ASEAN and Asian NIEs) as indices of higher technological industrialization in the manufacturing sector (Table 2-3).

Table 2-3 Comparison of Component Ratio of Capital Goods Imports

Country	1986	1990
India	35.6 (31.3)*	(23.3)*
Thailand	36.3	47.9
Singapore	43.0	48.9
Korea	42.0	41.7

Note*: Figures in ( ) were calculated from original figures in the Economic Survey 92-93 T.7.2 after deducting metal products, iron and steel.

Source: United Nations Statistical Year Book for Asia and the Pacific 1991.
Note: India's component ratio is lower than other countries, the reason of which is to be studied with relation to Factor 2 (domestic production) and Factor 11 (foreign exchange reserve), particularly in recent years.

(4) The rate of increase compared to the previous years is shown in Table 2-4.

Table 2-4 Rate of Increase/Decrease (%)

Years	I (Petroleum Oil)	II	III	Import Total
86/85	38.8 (42.9)	13.6	53.6	2.5
87/86	42.1 (42.8)	1.0	1.5	10.4
88/87	16.6 (7.5)	49.5	4.6	27.0
89/88	20.6 (44.1)	27.1	26.8	25.5
90/89	57.8 (74.2)	7.8	18.8	22.0
91/90	19.1 (21.2)	12.5	0	10.6

Note: Based on data from Table 2-1.

(a) The rate of increase of total imports has steadily decreased since 1989, primarily due to strict import restrictions under a serious foreign exchange reserves position (refer to Factor 11).

(b) Capital goods imports (Category III) mirror the trend of total imports, but Category II demonstrates an increase of 12.5 per cent in 1991 compared to 1990. The exports of Category II and III increased by Rs. 77 billion and Rs. 13 billion, respectively (refer to Factor 4). It can be surmised that the increase in the imports of Category II contributed to increased exports.

2.1.2 Export Trends

The structure of three categories of exported goods are examined and presented as a component ratio in Table 2-5.

Table 2-5 Composition of Goods Exported (%)

Year	I	II	III
1980	37.3	47.7	8.9
1985	40.7	51.8	6.4
1986	36.2	55.6	7.2
1987	31.4	61.5	7.0
1988	25.7	66.3	7.4
1989	22.8	65.9	8.7
1990	26.7	64.3	8.6
1991	25.6	65.0	9.3

Note: Based on the data from Table 2-1

(1) The ratio of Category I indicates a stable downward trend from 1986 to 1989, but in 1990 and 1991, demonstrated gains. According to statistic T.7.3 of the "Economic Survey 1992-93", such traditional items as tea, marine products, oil cakes, cashew kernels, and iron ore increased in recent years. However, as a long term trend, Category I demonstrated decreases; about 37.3 per cent in 1980, and measured a 29.8 per cent average for the past seven years.

(2) As for Category II, a ratio of 47.7 per cent in 1980 increased to a 61.4 per cent average for the last seven years; and this demonstrates a clear upward trend.

(3) Although the rate of increase is small, Category III demonstrated a stable upward trend. The average for four years from 1985 to 1988 is 7.0 per cent, but the last three years recorded an 8.8 per cent average.

(4) For reference, the component ratio of capital goods (Category III) for all exports was compared with selected ASEAN member countries and Asian NIEs, as an index of industrialization and the competitiveness of high value-added goods shown in Table 2-6.

Table 2-6 Comparison of Component Ratio of Capital Goods Export (%)

Country	1986	1990
India	9.9 (7.2)*	(8.6)*
Thailand	23.2	34.5
Singapore	46.7	54.2
Korea	35.7	41.4

Note*: Same as Table 2-3, except original statistic T-7.3
Source: Same as Table 2-3.

The component ratio of India is significantly lower than the other countries, especially compared to Thailand, a country primarily dependent upon agriculture that recorded a component ratio higher than Korea.

(5) The rate of increase compared to previous years is shown in Table 2-7.

Table 2-7 Rate of Increase/Decrease (%)

Year	I	II	III	Export Total
86/85	2.2	23.2	28.5	14.8
87/86	8.8	39.1	22.2	25.8
88/87	6.1	39.6	36.3	29.4
89/88	21.1	35.8	60.0	36.6
90/89	38.0	14.8	16.6	17.7
91/90	29.8	36.8	46.4	35.3

Note: Based on data from Table 2-1

(a) As per total exports, the rate has increased for the past five years, except for the figures reported in 1990. The same trend is observed in goods for Category II and III. These goods jointly have a substantial share of the component ratio (about 75 per cent), consequently this trend effects total export fluctuations. It appears that this trend will further accelerate in the future based on liberalized import and export promotion policies.

(b) Category II and III increases are associated with the changes in domestic production, consumption, and imports. This linkage will further strengthen in the future under the present policies of import liberalisation and export promotion. Present domestic production for Category II and III is to a considerable extent, dependent upon the imports of intermediate products, parts and components (the three items that belong to category II), and production equipment (Category III); and further the consumption trends effecting export-oriented businesses.

2.1.3 Domestic Production Trends

(1) The structural component ratio for three (Category I, II and III) production sectors is given in Table 2-8.

Table 2-8 Structural Component Ratio (%)

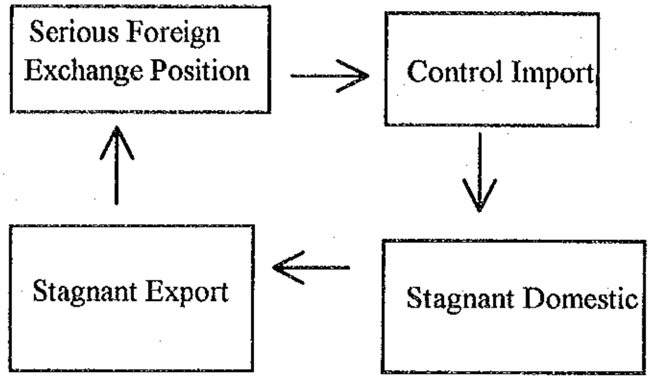
Year	I	II	III
1980	72	20	8
1985	68	23	9
1986	66	24	10
1987	65	25	10
1988	67	24	9
1989	66	25	9
1990	65	25	10
1991	65	25	10

Note: Based on data from Table 2-1

(a) The weight of Category I has dropped from 1980 to 1991, but Category II and III, have demonstrated a stable upward trend for each decade. This trend is forecasted to continue in the Eighth Five Year Plan period with active investments in infrastructure and manufacturing production.

(b) Substantial reform of the Import-Export Policy 1992-97, was announced in April 1992, which restructured the controls on imports to "free in principle", and is anticipated to stimulate capital goods imports and intermediate goods, with an expected linkage among active exports of manufactured goods. However, the country's foreign exchange reserve position, and the value of the Rupee in accordance with free market prices, are very important factors effecting this scenario.

(c) Domestic production trends for Category II and III sectors are closely associated with the country's foreign exchange revenue position, and directly associated with imports of such goods. This linkage is observed when imports are restricted due to reduced foreign exchange reserves. Reduced imports in critical sectors will slow domestic production in Categories II and III (which are dependent on imported materials, parts and components), and subsequently exports will fall, further reducing foreign exchange earnings. This linkage and its consequent effects can be illustrated on the following page.



Relationships Between Imports, Exports, and Foreign Exchange Reserves

(2) The rates of increase/decrease compared to previous years are shown in Table 2-9.

Table 2-9 Rate of Increase/Decrease (%)

Year	I	II	III	Total
86/85	-0.7	6.8	6.9	1.7
87/86	0.8	7.3	6.5	2.9
88/87	15.7	8.1	8.5	13.1
89/88	2.3	7.1	7.8	3.9
90/89	4.8	7.4	7.3	5.7
91/90	-1.0	-0.3	-1.0	-0.8

Note: Based on data from Table 2-1

(a) The production in Categories II and III demonstrated increasingly higher rates of growth than in each previous year between 1986 and 1988, but from 1989 the trend reversed and dropped to lower rates of increase (in 1991, growth rates for production in categories II and III, recorded decreases of 0.3 per cent and 1.0 per cent for each respective year). In 1991, not only these sectors, but Category I sectors also demonstrated a reduction (1.0 per cent), consequently the rate of increase for total production was 0.8 per cent in 1991.

(b) The reduction in growth rates for sectors in Categories II and III during the 1991 period, will be further analyzed utilising Table 2-4. Analysis revealed that after 1989, when imports of Category II and III began to drop, production in the same sectors followed this downward trend. This relationship suggests that industrial policies should be well-planned in order to reduce dependency on imported intermediate goods, manufactured products, and capital goods.

(c) Agriculture is the largest component of Category I, having approximately a 33 per cent share of GDP (five year period from 1985-86 to 1989-90, as is shown in Table 1.4 of the Eighth Five Year Plan). However, agricultural production is dependent and affected by year-to-year weather fluctuations. Consequently, a large variation in agricultural production is observed from Table 2-9.

2.1.4 Consumption Trends

Consumption trends were analyzed based on changes in gross domestic expenditure (GDE) figures. In this study, two important sectors of "private consumption" (approximately 65 per cent of GDE) and "gross fixed capital formation" (approximately 20 per cent), were adopted (as these factors combined occupied approximately 85 per cent of GDE).

(1) The component ratio for GDE, and the rates of change from the previous year for the two above factors, are shown in Tables 2-10 and 2-11.

Table 2-10 Component Ratio of Private Consumption and Gross Fixed Capital Formation (%)

Year	Private Consumption	Gross Fixed Capital Formation	Total	Notes
1980	72.1	19.2	91.3	of GDP in current prices
1985	67.1	20.7	87.8	
1986	67.2	20.9	88.1	
1987	66.7	21.3	88.0	
1988	65.5	21.0	86.5	
1989	65.0	21.4	86.4	

Source: Based on the United Nations "Statistical Year Book for Asia and the Pacific 1991".

Table 2-11 Changes from Previous Year (%)

Year	Private Consumption	Gross Fixed Capital Formation
1986/85	4.7	6.0
1987/86	4.2	6.4
1988/86	8.2	8.7
1989/88	0.8	8.4

Source: Based on Table 2-1

(2) Private Consumption

(a) Private consumption demonstrates a downward trend from 72.1 per cent in 1980, to 65.0 per cent in 1989, and gross fixed capital formation reveals a gradual upward trend from 19.2 per cent in 1980, to 21.4 per cent in 1989.

(b) The component ratio of private consumption (Table 2-10) and rate of increase for the previous year (Table 2-11), have decreased since 1985. The CPI in 1991 was 160 (1985 = 100), but consumption amounts increased only 40 per cent. This downward trend in private consumption, which occupies about 65 per cent of GDE, will in the future effect the development and growth of domestic production.

(3) Gross Fixed Capital Formation

Gross fixed capital formation demonstrates gradual incremental increases for the past ten year period, establishing a firm foundation for production activities for the future. However, there are concerns that deserve careful attention. It appears that domestic production in Category II and III is closely linked with the imports of these goods and the foreign exchange availability as observed in the "Trend of Domestic Production" (2.1.3-(4)). If difficulties occur effecting this linkage, gross capital formation will also be effected.

2.2 The Eighth Five Year Plan

2.2.1 Outline of the Plan

The Indian economy had stable growth at a rate of five per cent during the Sixth and Seventh Five Year Plan periods (1980-1990). However, a draft of the Eighth Five Year Plan, which was to begin in 1990, was not adopted due to domestic issues, and was instead inaugurated in 1992 for the five year period lasting until 1997.

The sectors most closely related to the IMT project are manufacturing, investment from foreign sources, and foreign trade, and are summarized below for planning purposes.

(1) Gross Domestic Production (GDP)

The GDP target growth rate (per cent per annum) is 5.6 per cent, about 0.3 percentage points higher than the growth rate achieved from 1985 to 1992. However, this GDP growth rate is 0.2 percentage points less than the Seventh Five Year Plan (1985-89) achievement of 5.8 per cent. (Refer to Table 2-12).

Table 2-12 Macro-Parameters for the Eighth Plan (1992-97)

Rates/Ratio	Seventh Plan (1985-90)	Seven Years including Seventh Plan (1985-92)	Eighth Plan (1992-97)
1. Rate of Growth in GDP (% per annum)	5.8	5.3	5.6
2. Domestic Saving (% of GDP)	20.3	20.7	21.6
3. Investment (% of GDP)	22.7	23.1	23.2
4. Current Account Deficit (% of GDP) 1)	2.4	2.4	1.6
5. ICOR (Incremental Capital Output Rate)	3.9	4.3	4.1
6. Growth Rate in:			
Export of Goods (% per annum)	8.1 2)	8.5 3)	13.6
Import of Goods (% per annum)	10.0	7.5 3)	8.4

Source: "Eighth Five Year Plan" Volume 1, Table 3.3
Government of India, Planning Commission
July 1992.

Notes: 1. In the Seventh Plan, the interest paid on NRI deposits was not included as part of the Current Account Deficit (CAD) because the RBI released the NRI capital inflow data after accounting for the interest paid. The CAD projection for the Eighth Plan includes the interest paid on NRI deposits as an item of imports of non-factor services.

2. This is estimated the five years of the Seventh Plan period. As per D.G.C.I. & S. quantum index, the estimates are 7.6 per cent for the Plan period, and 11.6 per cent during the last four years of the Seventh Plan.

3. This only represents a six year average because 1991-92 was an abnormal year in regarding foreign trade.

4. ICOR: Incremental Capital Output Rate

(2) Amount of Investment

(a) The Plan calls for total investments of Rs. 7,980 billion (23.2 per cent of normal GDP for the Plan period), out of which investment in the public sector amounts to Rs. 3,610 billion (refer to Table 2-13).

(b) Public sector investment is 45.2 per cent of the total (public and private) investment given in Table 2-14, and can be compared to the Seventh Plan achievement of 45.7 per cent, and the planned share of 47.8 per cent of total public sector investment. This decrease characterizes the basic principle of the Eighth Five Year Plan: substantial importance is given to the private sector.

Table 2-13 Sectoral Pattern of Investment and Financing in the Eighth Plan (1992-97)

(Rs.10 million at 1991-92 prices)

Sources of Financing the Investment		Investment					
S.No.	Sector	Own saving	Transfer from Household Sector's Savings	Rest of the world	Investment	Current Outlay	Aggregate Outlay
1.	Public Sector	68,900	258,400	33,700	361,000	73,100	434,100
2.	Private Corporate Sector	68,930	58,770	21,300	149,000		
3.	Household Sector	605,170	-317,170	--	288,000		
		743,000	--	55,000	798,000		

Source: "Eighth Five Year Plan" Volume 1, Table 3.5

Table 2-14 Share of Public Sector in Total Investment

	Public Sector Investment (as % of total investment)	
	Projected	Realised
Fifth Plan (1974-79)	57.6	43.3
Sixth Plan (1980-85)	52.9	47.8
Seventh Plan (1985-90)	47.8	45.7
Eighth Plan (1992-97)	45.2	--

Source: "Eighth Five Year Plan" Volume 1, Table 3.4

(3) Investment by Sectors

Investment by sectors is described in Table 2-15.

Table 2-15 Sectoral Investment during the Eighth Plan (1992-93 to 1996-97)

(Rs. 10 million at 1991-92 prices)

Sl. No.	Sector	Public	Private	Total	Share of Public Sector in Total Investment by Sectors (%)	Sectoral Distribution		
						6th Plan	7th Plan	8th Plan
1.	Agriculture	52,000	96,800	148,800	34.95	15.24	11.23	18.65
2.	Mining & Quarrying	28,500	11,100	39,600	71.97	6.06	6.70	4.96
3.	Manufacturing	47,100	141,300	188,400	25.00	23.60	26.00	23.61
4.	Electricity, Gas & Water	92,000	10,120	102,120	90.09	12.07	13.65	12.80
5.	Construction	3,300	17,240	20,540	16.07	2.73	1.86	2.57
6.	Transport	49,200	38,710	87,910	55.97	9.42	9.93	11.02
7.	Communication	25,000	1,000	26,000	96.15	1.50	2.03	3.26
8.	Services	63,900	120,730	184,630	34.61	29.38	28.60	23.13
	Total:	361,000	437,000	798,000	45.24	100.00	100.00	100.00

Note:Sixth & Seventh Plan figures are calculated at 1980-81 prices.
Source: "Eighth Five Year Plan" Volume 1, Table 3.15

(a) Agricultural investment comprises 18.65 per cent of total public sector outlays, with the most substantial increase among the sectors documented in the Eighth Plan. However, in the Seventh Plan, agricultural investment decreased to 11.23 per cent from 15.24 per cent provided in the Sixth Plan.

(b) The agriculture sector is the largest component of GDP (about 33 per cent for the 1985-90 period), and has an overall impact on other sectors via input linkages such as employment (about two-thirds of the work force were employed in agriculture for this period), consequently, stable agriculture growth is an important strategy for GDP growth.

(c) The manufacturing sector is the largest sector garnering investments (Rs. 1,884 billion is planned for investment), and accounts for 23.61 per cent of total investment in the Eighth Plan (refer to Table 2-15). The investment distribution for the public and private sectors is 25 per cent and 75 per cent, respectively.

(d) Infrastructure such as electricity, gas, and water comprise 12.8 per cent of public sector investments; transport receives 11.02 per cent; and communication 3.26 per cent (about 27.08 per cent of total public sector investment). In the Seventh Plan, infrastructure investments were 25.6 per cent, and in the Sixth Plan, 23.0 per cent. Compared to previous central government budgetary plans, the Eighth Plan attaches significant importance to infrastructure; an essential foundation for future economic growth.

(e) From Table 2-15, the public sector comprises 45.24 per cent of total public investments; thus the private sector receives 54.76 per cent of total public shares; the remaining amounts are reserved for the private sector. In the private sector, manufacturing occupies 32.33 per cent, and the services sector, 27.62 per cent; for a total of 59.95 per cent.

This portends strong government intentions to stimulate the private sector, especially the manufacturing and service industries. This relationship can be observed in the liberalization and privatization policies stressed in the New Industrial Policy 1991, the EXIM Policy 1991, and various subsequent policy announcements for the structural adjustment of the nation's economy.

(4) Sectoral Growth Rate

The sectoral growth pattern in the Eighth Plan is presented in Table 2-16.

The sectoral growth rate of GVA from 1981-82 to 1990-91 was 9.0 per cent for electricity, gas and water, and 7.3 per cent for transport, and 7.2 per cent for manufacturing.

In the Eighth Five Year Plan, mining achieves the largest growth rate at 8.0 per cent, followed by electricity, gas, and water (7.8 per cent), and transport (6.7 per cent). Compared to these sectors, manufacturing is at a relatively higher rate (7.3 per cent) than in the Seventh Plan.

According to the value of gross output, the manufacturing sector is projected to grow 8.2 per cent following the highest growth rate of 8.9 per cent in mining, consequently the sectoral share of manufacturing in GDP is estimated at 23.3 per cent in the last year (1996-97) of the Eighth Plan. As this figure indicates, the role of manufacturing in the Eighth Plan becomes significant.

Table 2-16 Sectoral Growth Rates of Gross Value Added at Factor Cost (GVA) and Value of Gross Output

Sl. No.	Sector	Trend Growth Rate of G.V.A. 81-82 to 90-91 (10 years)	Projected Growth Rate 92-93 to 96-97 (per cent per annum)		Sectoral Share in GDP (Percent)	
			G.V.A.	Value of Gross Output	1991-92	1996-97
1.	Agriculture	3.8	3.1	4.1	27.7	24.6
2.	Mining & Quarrying	6.8	8.0	8.9	2.0	2.3
3.	Manufacturing	7.2	7.3	8.2	21.5	23.3
4.	Electricity, Gas & Water	9.0	7.8	7.6	2.4	2.7
5.	Construction	3.6	4.7	5.3	5.1	4.9
6.	Transport	7.3	6.7	7.7	5.9	6.2
7.	Communication	6.2	6.1	6.9	1.2	1.2
8.	Other Services	6.5	6.0	6.6	34.2	34.8
9.	Total	5.6	5.6	6.7	100.0	100.0

Source: "Eighth Five Year Plan" Volume 1. Table 3.14

2.2.2 Balance of Payments

The balance of payments projections for the Eighth Five Year Plan period are given in Table 2-17.

(1) Trade Account

(a) India's trade account has historically suffered beginning with the First Five Year Plan, 1950-1955 (except 1972 and 1976). The deficit rate (export amount/import amount) was recorded at 56.4 per cent in the 1960's; 19.6 per cent for the 1970's; 63.7 per cent during the first half of the 1980's; 44.5 per cent during the latter half of the 1980's; 32.7 per cent in 1990; and 40.7 per cent in 1991 (refer to Table 2-17).

Table 2-17 Balance of Payments Position during the Eighth Five Year Plan (1992-97)

(Rs.10 million)

	1991-92	1996-97	Total 8th Plan
Exports	44,292	83,869	330,153
Imports*	62,345 (51,700)	93,314	399,650
Trade Balance*	(-)18,053	(-)9,445	(-)69,497
Invisible*	3,494	2,332	14,634
C.A.D.*	(-)14,559 (7,000)	(-)7,113	(-)54,863

Notes*: These are normalised projections for the base year. Actuals during 1991-92 are lower, as indicated in brackets and later explained.
Source: "Eighth Five Year Plan" Volume 1, Table 3.28.

(b) The Eighth Five Year Plan projected exports to total Rs. 3,301.5 billion, and imports for the Plan period at Rs. 3,996.5 billion. Consequently, the trade deficit will be about Rs. 695 billion (21 per cent deficit rate). However, the deficit rate during the last year of the Plan period is projected to decrease to 11.2 per cent .

(c) During the Seventh Plan period, the performance of exports amounted to Rs 869 billion, imports Rs. 1,256 billion, and a trade deficit of 387 billion (44.5 per cent deficit rate).

(d) In the Eighth Plan, the trade deficit increases to Rs. 695 billion, about 80 per cent larger than the Seventh Plan period deficit. However, exports increase 3.8 times and imports 3.2 times from the Seventh Plan results. During the Eighth Plan period, it appears export and import activity will be significantly improved.

(2) Current Account

(a) The current account deficit (CAD) is Rs 548.6 billion (refer to Table 2-17), and corresponds to 1.6 per cent of GDP (refer to Table 2-19) in the Eighth Plan. The CAD for the Seventh Plan period was 2.38 percent and 1.43 percent during the Sixth Plan. The Eighth Plan will significantly improve compared to the Seventh Plan, but remain less than achieved during the Sixth Plan.

(b) An important factor effecting the current account is the invisible account (non-trade). Table 2-19 reveals that the invisible account surplus (invisible net) was 1.90 per cent of GDP during the Sixth Plan. During the Seventh Plan, the invisible account dropped to 0.75 per cent, and is expected to hit 0.42 per cent during the Eighth Plan period.

(c) Analysing India' current account is possible by observing the trade and non-trade accounts, and it appears that the invisible net could reduce the trade account deficit. Calculations based on the value of the Rupee from the "Economic Survey 192-93", Table 6.3 (A) s-79, and Table 7.1 (A) S-84, demonstrated that the rate of reducing the deficit (invisible net/trade account deficit) was 35.7 per cent in 1980; averaged 44.2 per cent in 1985-87; and 24.6 per cent in 1988 (based on the U.S. dollar, the rate is 14.5 per cent - refer to Table 2-18). However, after 1989, the data did not directly demonstrate such a pattern.

As shown in Table 2-18 (U.S. dollar), after 1989, the rate of the invisible net to reduce the CAD was 8.2 per cent, 0.2 per cent for 1990, and 1.7 per cent in 1991.

Table 2-18 Trade Balance

(US $ million)

Account	88-89	89-90	90-91	91-92
Trade Balance	-9,361	-7,456	-7,750	-3,078
Invisible (net)	1,364	615	23	52
Current Account	-7,997	-6,837	-7,727	-2,835

Source: Economic Survey 92-93. (Table 5-1 rearranged)

Table 2-19 Key Indicators of India's Balance of Payments (as per cent of G.D.P.)

Year/Period	Exports	Imports	Trade Balance	Net Invisible	Current Account Deficit
Average (1980-85)	5.00	8.33	-3.33	1.90	1.43
Average (1985-90)	5.21	8.33	-3.33	0.75	2.38
Eighth Plan (1992-97) Projections	9.60	11.62	-2.02	0.42	1.60

Source: "Eighth Five Year Plan" Volume 1, Table 3.27.

(d) In an attempt to reduce CAD, it appears necessary to reduce the trade account deficit and increase the non-trade account surplus. The net income of the non-trade account items are listed in Table 2-20. From the table it was observed that the largest income item was private transfers payments (primarily remittances by Indian labourers in the Middle East countries), totaling Rs 20.0 billion in 1980, and Rs 38.4 billion in 1988. However, Indian nationals working in that region were forced to return home during the Gulf War in 1990-91, and could be a significant cause of the recent foreign exchange shortage.

Table 2-20 Net Income of Non-Trade Account

(Rs. Million)

Account Items	1988-89	1989-90	1990/Jan.-June
Travel	146	171	112
Transportation	-18	-34	-09
Insurance	04	05	07
Investment Income	-364	-487	-265
Gov't (not included elsewhere)	-09	-15	-09
Miscellaneous	-16	-06	-11
Transfer Payments			
Official	72	89	47
Private	384	379	241
Invisible Net Total	197	102	113

Source: The Reserve Bank of India, Monthly Bulletin. March 1993

(e) The travel account item is the second largest revenue source in the invisible account, and is more stable as an income source than transfer income from overseas workers. Revenues generated from tourism could provide additional revenues as India reported 1.5 million foreign tourists in 1991. However, the number of tourists visiting India is less than reported for Singapore (six million) and Thailand (five million).

(3) Financing Current Account Deficit

(a) Financing of the current account deficit in the Eighth Plan mentioned above is projected at Rs. 550 billion, and is shown in Table 2-21.

Table 2-21 Financing the Current Account Deficit

		Seventh Plan (Rs. crores at Current prices)	Eighth Plan (Rs. crores at 1991-92 prices)
1.	Current Account Deficit including Errors & Omissions Financed by	42,284	55,000
2.	External Assistance including official transfers*	10,572	28,700
3.	Commercial Borrowings	10,592	5,000
4.	Non-Resident Deposits	10,164	3,000
5.	Other Capital	5,879	21,300
6.	Use of Reserves	(-)5,077	3,000

* Net of repayments to IMF and others
Source: "Eighth Five Year Plan" Volume 1, Table 3.29

(b) In the Seventh Plan, the CAD (Rs. 422 billion) was financed by external assistance, (25 per cent), commercial borrowing (25 per cent), non-resident deposits (24 per cent), direct investment (14 per cent), and additional expenditures of foreign exchange reserves (13 per cent).

(c) In the Eighth Plan, as in Table 2-21, the financing pattern substantially changes, and CAD is projected to reduce from external assistance (52.18 per cent of the total amount) and direct investment (38.72 per cent); 90 per cent of the total deficit.

(d) Dependency on commercial borrowing drops to 9 per cent, consequently foreign exchange reserves will increase by Rs 30 billion at the end of the Plan period.

(4) Export and Import Projections

(a) Total exports for the Eighth Plan period are projected at Rs. 3,301.5 billion, and export commodities were classified into three groups: agricultural and allied products; ores and minerals; and manufactured goods. The first and second classifications occupy 19 per cent of total exports, and as commodities are primary products, raw materials, and processed products. The third classification, manufactured goods, occupies 76 per cent.

(b) Export promotion is an important trade strategy issue in the Eighth Plan, and the growth rate is expected to be 13.6 per cent per annum. Primary products projected gains in foreign exchange are anticipated by increasing exports of traditional items such as marine products, oil cakes, cashew kernels, sugar, spices, rice, vegetables, fruits, and processed foods. A difficulty the government faces is increasing production in these areas in order to generate adequate surpluses for export.

(c) Manufactured goods exports are expected from traditional chemicals, ready-made garments, cotton yarn and clothes, leather and leather manufactured goods, gems and jewelry and handicrafts. In addition, exports of iron and steel, cement and sugar, the production capacity of which was increased by large scale investments in these industries, are also expected to increase.

(d) Total imports in the Eighth Plan period are projected at Rs. 3,996.5 billion. The import commodities are classified into two groups according to import projections (Table 3-30, in the Plan Paper). Specifically, bulk items (39 per cent of total imports), and all others (60 per cent share). Rearranging the commodity classifications from an industrial and trade strategy view point, crude materials occupy 32 per cent of total imports, and intermediate and manufactured goods, 68 per cent[1].

(e) The import requirements of major export commodities were planned on the basis of the level of import dependency, the possibility of import substitution by domestic products, and export targets. As for capital goods imports, requirements were identified based on past import relationships with domestic fixed capital formation, gross value-added, and industrial production.

(f) The decline in domestic production of crude oil in the initial years of the Plan, coupled with the slower build up of crude oil refining capacity, makes it necessary to adequately provide for imported oil and petroleum products (which account for about 20 per cent of total imports). It is also predicted that this will require

[1]Note: These composition ratios were calculated according to Table 3-30 ("Import Projections for the Eighth Plan", The Eighth Five Year Plan, 1992-97 The Government of India. page 81. On the basis of Rs. 3,445 billion (E: Grand Total Rs. 3,996.5 billion; D: Statistical Adjustments Rs. 551.0 billion).

restraining imports of other commodities, particularly capital goods and transport equipment.

2.3 Central Government Budget for 1993-94

New Budget for 1993-94 was presented by the Minister of Finance on February 28, 1993.

2.3.1 Budget Outline for 1993-94

(1) Deficit Target Reduction

The deficit rate, as a part of GDP requested by the IMF, is 5.0 per cent for 1992-93, but is expected to be 5.25 per cent as a result of the government's efforts to minimize the deficit. (The deficit for 1991-92 was 6.2 per cent)

(2) Deficit Budget Amounts

Estimates of total revenues for the 1993-94 budget year are Rs. 1,270 billion, and expenditures are Rs. 1,313 billion from Table 2-22. Consequently, the budget deficit is estimated at Rs. 43 billion, the lowest for the past decade.

(3) Public Plan Expenditures

However, the central plan outlay (budget support Rs. 232 billion, and internal and external budgetary resources of public enterprises, etc., Rs. 406 billion, total Rs. 638 billion) was increased by 32 per cent more than this year's budget (1992-93), and portends that the central government has confidence in managing the macro-economy, and is not following an economic policy of simply reducing the deficit. Budgetary support for public sector enterprises increased 26 per cent (from this year's Rs. 185 billion to Rs. 232 billion) for the next year.

(4) Inflation Rate

Reduction of the fiscal deficit (borrowed funds and other liabilities, plus the budget deficit) is a critical problem for the government during the next year; especially if the central government is to successfully control inflation. In this budget, the ratio of fiscal deficit to GDP is set at 4.75 per cent, assuming a GDP growth rate of 5.0 per cent and an inflation rate of 8.0 per cent.

(5) Revenue

Revenue receipts are Rs. 842 billion, 7.6 per cent more than the revised budget estimates of 1992-93.

Tax revenues are estimated at Rs. 627 billion, 7.8 per cent more than this year, but it appears that the government expects to balance the reduction in revenue receipts due to custom duty and excise rates reductions by an increase in direct tax revenues from economic growth and expected export and import trade expansion. (Note: This year's tax revenue is estimated at Rs. 581 billion, about Rs. 17 billion more than the 1992-93 budget estimates.)

(6) Expenditures

The non-plan expenditures (Rs. 900 billion) increased only 2.6 per cent compared to the 1992-93 revised estimates (Rs. 877 billion). This occurred because loans to the state governments and the Union Territory were cut 9.0 per cent (from Rs. 48 billion of the 1992-93 revised budget estimates) to Rs. 44 billion. Other important items, such as defense expenditures and capital expenditures increased 9.6 per cent more than the 1992-93 revised estimates, and occupy 14.6 per cent of total expenditures for the 1993-94 budget.

(Revenues and expenditures for the past three years are given in Table 2-22, and are quoted from "Budget at a Glance; 1993-94", the Ministry of Finance. Government of India.)

Table 2-22 Budget at a Glance[2]

(In Rupees Crore)	1991-92 Actual	1992-93 Budget Estimates	1992-93 Revised Estimates	1993-94 Budget Estimates
1. **Revenue Receipts**	66,047	75,688	78,279	84,209
2. Tax Revenue (Net to Centre)	50,070	56,456	58,179	62,739
3. Non-Tax Revenue	15,977	19,232	20,100	21,470
4. **Capital Receipts**	38,528	38,010	39,245	42,800
5. Recoveries of Loans	6,020	6,491	6,225	6,655
6. Other Receipts	3,038	2,500	3,500	3,500
7. Borrowings and other liabilities	29,470	29,019	29,520	32,645
8. **Total Receipts (1+4)**	104,575	113,698	117,524	127,009
9. **Non-Plan Expenditure**	80,469*	84,475	87,753	90,072
10. On Revenue Account of which	67,234*	71,233	74,461	77,654
11. Interest Payments	26,563	32,000	32,500	38,000
12. On Capital Account	13,235	13,242	13,292	12,418
13. **Plan Expenditure**	30,961	34,612	36,973	41,251
14. On Revenue Account	15,074	18,337	20,518	24,185
15. On Capital Account	15,887	16,275	16,455	17,066
16. **Total Expenditure (9+13)**	111,430	119,087	124,726	131,323
17. Revenue Expenditure (10+14)	82,308	89,570	94,979	101,839
18. Capital Expenditure (12+15)	29,122	29,517	29,747	29,484
19. **Revenue Deficit (1-17)**	16,261	13,882	16,700	17,630
20. **Budgetary Deficit (8-16)**	6,855	5,389	7,202	4,314
21. **Fiscal Deficit [(1+5+6)-16=7+20]**	36,325	34,408	36,722	36,959
22. **Primary Deficit (21-11)**	9,762	2,408	4,222	(-)1,041
Increase in net RBI Credit to Central Government #	5,508	5,389	5,400	4,314##

Source: "Budget at a Glance: 1993-94." The Ministry of Finance, Government of India.

[2]Note: *= Includes grants under Article 275 (1) of the Constitution for Meeting Plan Expenditure.
= Including other variations in Reserve Bank of India's credit to the Central Government.
= Not independently examined.

2.3.2 Main Policies Announced in the Budget

The essential characteristics of the central government's new economic policies announced February 28, 1993, in the Finance Minister's budgetary speech are as follows:

(1) Full Convertibility of the Rupee for the trade account

The 1993-94 Budget has unified the exchange rate to convert 100 per cent foreign exchange earnings at the market rate from March 1, 1993 in place of the partial convertibility system (40 per cent at the RBI official rate) introduced in last year's budget announcement.

(2) Custom Duty Reductions

(a) The auxiliary duty was merged with the basic duty in order to simplify the tariff structure and assessment process.

(b) The maximum level of 110 per cent was reduced to 85 per cent for custom duty.

(c) The reduction scheme for main import items can be referred to in Table 2-23.

The loss of revenue by this reduction amounts to Rs. 32.7 billion.

Table 2-23 Custom Duty Reductions

Item	(From)	(To)
Project Machinery for Coal & Petroleum Sector	30%	25%
Project Equipment	55%	35%
Power Projects (also extended to machinery required for modernization & renovation)	30%	20%
Capital Goods for Leather, Textiles, Marine Products GEM & Jewelry	40%	25%
Components of General Machinery	35-40%	25%
Various Types of Machine Tools & Instruments		40,60, 80%
Steel Scrap	20%	15% (up)
Non-Ferrous Metals (unwrought and unalloyed forms)		25% - 50%
Non-Ferrous metals (wrought forms)		70-80%
Specified Pesticides	110%	75%
Chemicals		uniform rate 15% DMT, PTA & MEG 70%
Electronics Project, Capital Goods for Electronics	30-50%	25%
Raw Materials & Parts for Electronics	40-80%	20,35, 50%
Specified Raw Materials for Optical Fiber Cable	90%	20%
Fishing Equipment	40%	15%
Film Rolls	55,65, 35%	25, 40, 25%
Specified Bulk Drugs		25%
Sealing Machines for Packing Intravenous Liquids	40%	15%

(3) Excise Duty Reductions

The following items will have an excise duty reduction.

(a) This reduction for consumer goods such as tea, coffee, vanaspati, biscuits, soap, footwear, cosmetics, etc., should encourage domestic consumer consumption.

(b) The excise duty rates for automobiles, refrigerators, air conditioners, capital goods, etc., were reduced.

(c) The reduction scheme for main commodities is referenced in Table 2-24.

Excise duty reductions amounted to Rs. 12.4 billion deficit in revenues.

Table 2-24 Excise Duty Reductions

Coffee, Tea & Instant Tea	Fully	exempted
Vanaspati	From Rs. 1,990	to Rs. 1,500 p.m.t.
Footwear Specified Units	Fully	exempted
Evaporative Coolers	From 23%	to 10%
Electric Fans	17.25%	to 10%
Domestic Electrical Appliances	23%	to 15%
Dry Cell Batteries	34.5%	to 25%
Printing & Writing Ink	17.25%	to 10%
Radio Sets	23%	to 10%
Tooth Powder	17.25%	to 10%
Noodles & Roasted Coreals	17.25%	to 10%
Biscuits	11.25%	to 7.5%
Plastic Molded Luggage	34.5%	to 25%
Mattresses & Bedding Articles of Cellular Rubber	69%	to 30%
Capital Goods & Instruments	11.5% to 23%	to 10%
Capital Goods & Instruments (Power Sector)		to 5%
Non-Petrol Driven Vehicle	23%	to 15%
Three Wheelers	23%	to 15%
Motor Cars	55%	to 40%
Colour Television	Rs. 1,925 to Rs. 4,785	Rs. 1,250 to Rs. 2,200
Refrigerators	Rs. 575 to 5,750	Rs. 400 to 3,500
Refrigerators for Cold Storage	69%	20%
Air conditioner	Rs. 13,800 to Rs. 8,500	Rs. 7,000 to Rs. 70,000
A.C. Compressors upto 7.5 Tonnes	Rs. 6,900	to Rs. 5,500
Bulk Plastic Resin	46%	to 35%
Ferrous Metal	11.5% to 23%	to 12.5% to 15%
Aluminum	23% to 40.25%	to 25%
Non-Ferrous Metal	11.5% to 34.5%	to 15%
Plywood	34.5%	to 20%
Cosmetics & Toiletries	120.75%	to 70%
Molasses	Rs. 172.50	to Rs. 200 P.M.T.

(4) Corporate Tax and Income Tax Rates

The central government deferred action on the Chelliah Committee recommendation to gradually reduce corporate and income tax rates, and thus, a reduction was not proposed. The government is primarily trying to reduce the budget deficit which will in turn reduce the rates of indirect taxes. Consequently, there are funding difficulties with an attempt to reduce direct taxes under the new budget (this was discussed by the Finance Minister in the budget speech).

(5) Tax holiday for new investments to backward areas and particular sectors

In order to stimulate investment in industrially backward areas, infrastructure such as electricity, and industrial areas specialising in electronic products (electronic hardware technology parks), the budget proposed a five-year tax holiday.

The expected revenue loss by this measure totals about to Rs. 3 billion.

(6) Permission for nationalized banks to access directly the capital market for funds.

The government has decided to permit the State Bank of India and other nationalized banks to directly access the capital markets for funds to overcome capital scarcity in addition to the budgetary capital allocations (Rs. 57 billion). However, the government will continue to retain its majority ownership in the banks, and consequently will keep effective management control.

(7) Reduction of Interest Rates

From March 1, 1993, interest rates reductions will commence.

(a) The maximum interest rate on bank deposits was lowered to 11 per cent from 12 per cent.

(b) The minimum lending interest rate on commercial advance was reduced to 17 per cent from 18 per cent.

(c) To promote exports, the export financing interest rate was reduced to 13 per cent from 14 per cent, and the interest tax was waived. Also, banks were required to allocate 10 per cent of total lending for export financing.

(8) Reduction of SLR (Statutory Liquidity Ratio)

The effective average level of the SLR at present is about 38 per cent, which was decided for reduction to 37.75 per cent, and will be further reduced to 25 per cent during the next three years. This reduction will eliminate a large portion of banks resources from below market rates of interest.

(9) Central Plan Outlay Increase

A sharp increase in the central plan outlay of Rs. 155 billion more than the 1992-93 budget estimates (Rs. 484 billion) to Rs. 639 billion, was announced to finance increased expenditures for rural development, and for crucial infrastructure sectors such as education, welfare, transport, energy, et cetera.

At the same time, the government will dispose (divest) of shares held in the public sector enterprises and obtain Rs. 35 billion in funds.

(10) Increasing the Standard Income Tax Reduction Level for Individual Income

(a) For salaried incomes, the standard reduction was increased to Rs. 15,000 from Rs. 12,000.

(b) For working women with incomes up to Rs. 75,000, the standard reduction increased to Rs. 18,000 from Rs. 15,000.

(c) For the elderly, a tax rebate increased to 20 per cent from its previous 10 per cent level, and the income ceiling was also increased to Rs. 75,000 from Rs. 50,000.

(d) The gift-tax exemption ceiling increased to Rs. 30,000 from Rs. 20,000.

CHAPTER 3 TRADE AND INDUSTRIAL PROMOTION POLICIES

CHAPTER 3 TRADE AND INDUSTRIAL PROMOTION POLICIES

3.1 Industrial Promotion Policy: Trends

In order to correctly understand the importance of the New Industrial Policy, 1991 (NIP 91), it is necessary to have an understanding and historical background of the government's role in India's economic activities following independence. Therefore, the objectives of past policies are briefly described below.

3.1.1 Prior to the New Industrial Policy of 1991

After gaining independence, the Indian government's basic industrial policy was directed at developing the country's primary manufacturing industries. Consequently, industrial policy was formulated to: (1) protect domestic industries; (2) control foreign capital investments; 3) provide the public sector with the domination and monopoly of core industries; and (4) restrain the private sector's activities through a rigorous licensing and industrial approval system.

India's economic system was patterned after a "mixed economic" approach. Simply stated, India's mixed economy utilised socialistic and capitalist economic principles that led to a strong administrative and centrally controlled economy. From this, it can be observed that the country's arrested economic development and critical foreign exchange position are closely related to the country's administratively controlled economic structure.

In an attempt to restructure the country's economy, the Narashimha Rao Cabinet announced in rapid succession, substantial reform of the country's industrial and trade policies beginning in July 1991. A summary follows:

*	New Industrial Policy 1991 (NIP)	:	announced in July 1991
*	New EXIM Policy 1991 (EXIM)	:	announced in July 1991
*	Import and Export Policy 1992-97	:	announced in March 1992
*	Amendment of the Foreign Exchange Regulation Act (FERA) 1973	:	announced in January 1993
*	Announcement of the 1993-94 Budget for 1993-94, and new economic policies	:	announced in February 1993

The New Industrial Policy 1991, can be historically placed in comparison to past progress of industrial policies and economic control measures applied by the government since independence. This section, "Prior to the New Industrial Policy 1991", was prepared for that purpose.

(1) Industrial Policy Resolution (IPR) 1948:

Provides the operative spheres of the public and private sectors, and clarifies which public sector enterprises are directly controlled by the Central Government.

(2) Industries' Development and the Regulation Act (IDRA), 1951:

Licensing systems for the private sector were introduced, and control of industrial operations was established in line with the IDRA 1951; subsequent Acts strengthened the government's position and are listed below:

(a) Capital Issue Control Act, 1947 to 1955: Control at the issuance of stocks and bonds.

(b) Essential Commodities Act, 1955, which controlled prices, distribution, and supply of important commodities such as iron, steel, coal, fertilizer, et cetera.

(c) Company Act, 1956.

(d) Monopolies and Restrictive Trade Practices Act, 1969 (MRTP).

Enacted to decentralise economic power and deter monopolistic, restrictive, and unfair trade practices. This act was enforced in addition to the IDR 1951. By this Act, government reinforced the licensing system for establishment of new undertakings, expansion of undertakings and mergers, especially large scale companies that could dominate markets.

(e) Foreign Exchange Regulation Act, 1973 (FERA)

This act controlled a foreign company's business activities in the Indian domestic economy, and allowed foreign equity ownership only up to 40 per cent in a company.

(3) Industrial Policy Resolution (IPR), 1956

This resolution modified the 1948 Industrial Policy Resolution and the public sector became a dominant economic force. Industries were classified into three groups (Schedules A, B, and C).

Schedule A:	Industries under monopolistic control by the public sector. Arms and ammunition; atomic (nuclear) energy; railway transportation; mining (coal, oil, iron ores, etc.); manufacturing (iron and steel, heavy casting and forging, heavy machinery, heavy electric machinery, aircraft, shipbuilding, telephone, and telegraph equipment); air transport, electrical power generation, power transmission, and distribution.
Schedule B:	Public and private sector industries which were gradually nationalised and reserved for the public sector. Aluminum, machine tools, special steels and alloys, mining, roads and marine transport.
Schedule C:	Industries reserved for the private sector. All other industries not classified as Schedule A or B.

(4) Industrial Policy Government Decisions (IPGD), 1973:

Established to correct excessive administrative control in the industrial sphere, and expanded the production activities of large domestic undertakings and foreign enterprises approved for active participation by foreign and domestic enterprises in Schedule A, B, and C stated above. However, this has not basically altered towards a market-oriented economy.

(5) The Government's Industrial Policies in 1977, 1980, and 1982:

(a) Industrial Policy: 1977

Janata Party (currently the Baharatia Janata Party: BJP. BJP terminated within two years.) promoted policy decisions to alleviate control on essential industrial goods.

(b) Industrial Policies: 1980, 1982

During the Indira Gandhi government, India's foreign exchange reserves position deteriorated. To forestall any further foreign exchange deterioration, the central government sought assistance from the International Monetary Fund (IMF). The IMF agreed to provide funding to the government provided that economic liberalisation efforts were promoted. However, research indicates that the government did little, if anything, to further economic liberalisation in the country.

Rajiv Gandhi's Cabinet in 1985, professed economic and industrial liberalisation policies, but failed to enact legislative measures, promote liberalisation, and enlist the cooperation of the central and state government bureaucracies. It appears that failure to sufficiently promote liberalisation policies may have led to the country's critical foreign exchange reserves position in 1990 and 1991.

3.1.2 New Industrial Policy, 1991 (NIP 91)

The New Industrial Policy was announced July 24, 1991, and approved August 26, 1991. The NIP 91 was the central government's attempt to promote foreign investment to the country and restructure the country's industrial economy. Article 39 of NIP 91, best states the central government's intentions: (The) "Government has decided to take a series of measures to unshackle the Indian industrial economy from the cobwebs of unnecessary bureaucratic control."

NIP 91 is organised into five articles and is summarised below.

(1) Industrial Licensing Policy
(2) Foreign Investments
(3) Foreign Technology Agreements
(4) Public Sector
(5) The Monopolies and Restrictive Trade Practices Act (MRTP)

(1) Industrial Licensing Policy:

(a) Areas where security and strategic concerns predominate will continue to be reserved for the public sector (eight industries, list attached as Annex. I of Appendix II).

(b) For all industries, except 18 core industries (list attached as Annex. II of Appendix II), licensing will be abolished. However, industries reserved for the small scale sector will continue to be under licensing.

(c) All existing registration schemes (De licensed Registration, Exempted Industries Registration, DGTD registration) will be abolished.

(d) For new projects and substantial expansion, entrepreneurs will henceforth only be required to file an information memorandum.

(e) In locations other than cities with a population of more than 1 million, industrial approval by the central government will not be required; except for industries subject to compulsory licensing.

In those cases where the location of an industry is in cities with population of more than 1 million, pollution industries will be located 25 km from the external boundary, except in prior designated industrial areas such as electrical, computer software, printing, et cetera.

(f) In projects where imported capital goods are required, automatic clearance will be given, for those cases where:

i) foreign exchange availability is ensured through foreign equity, or

ii) if the CIF value of imported capital goods is less than 25 per cent of the total value of plant and equipment, upto a maximum value of Rs. 2 crores.

In other cases, clearance from the Secretariat of Industrial Approvals (SIA) will be required. Existing units will be permitted to expand product items without additional investment. The licensing exemptions will apply to all substantial expansion of existing units.

(g) The system of Phased Manufacturing Programmes (PMP: Policy for increasing the domestic procurement rate) will not be applicable to new projects; existing projects under the PMP system will continue to be governed accordingly.

(h) The Mandatory Convertibility Clause will no longer be applicable for term loans from financial institutions for new projects.

(2) Foreign Investment

(a) Approval will be given automatically for direct foreign investment upto 51 per cent from 40 per cent foreign equity in high priority industries (34 industries, list attached as Annex. III of Appendix II), for those cases where foreign equity covers foreign exchange requirements for imported capital goods.

(b) To provide access to international markets, trading companies primarily engaged in export activities will be allowed majority foreign equity holdings to 51 per cent.

(c) The payment of dividends will be monitored through the Reserve Bank of India (RBI) so as to ensure that outflow on accounts of dividend payments are balanced by export earnings over a period of time.

(d) A Special Empowered Board (SEB) will be constituted to negotiate with a number of large international firms and approve direct foreign investment in selected areas. The investment programmes of such firms will be considered free from predetermined procedures.

(e) For the importing of capital goods, where foreign exchange availability is insured through foreign equity, the import license will be given automatically.

(f) For the importing of capital goods, if the CIF of the imported capital goods is less than 25 per cent of the net total value of plant and equipment, (up to a maximum value of Rs. 20 million) an import license will be automatically granted.

(3) Foreign Technology Agreement

(a) Automatic permission for payment of royalty will be given for foreign technology agreements in high priority industries (Annex III, Appendix II), subject to:

i) upto a lumpsum payment of Rs. 10 million

ii) 5 per cent royalty for domestic sales
iii) 8 per cent royalty for exports.

In the case of ii) and iii) (royalty on sales), the total amount of payments shall be less than 8.0 per cent of sales for a 10 year period from the date of an agreement, or 7 years from commencement of production.

(b) For industries other than those in Annex III of Appendix II, automatic permission will be given subject to the same guidelines as above if free foreign exchange is not required for payment. All other proposals will need specific approval under the general procedures in force.

(c) No permission will be necessary for the hiring of foreign technicians, foreign testing of indigenously developed technologies.

(4) Public Sector

(a) Industries related to security and strategic concerns (eight industries listed attachment as Annex I of Appendix II) will be operated in the public sector, but the private sector will be selectively given an opportunity in this area. However, the public sector will be permitted to enter in areas not reserved for it.

(b) Public enterprises which are chronically sick and which are unlikely to be rehabilitated, will be referred to the Board of Industries and Financial Reconstruction (BIFR).

(c) A part of the government's share holdings in the public sector will be offered to mutual funds, financial institutions, the general public, and workers in order to introduce the private sector's economic vitality into the public sector.

(d) The autonomy and authority of public sector enterprises will be expanded and management will become more professional.

(5) MRTP Act

(a) The MRTP Act will be amended to remove the threshold limits of assets in respect of MRTP companies and dominant undertakings.

(b) This eliminates the requirement of prior approval of the central government for establishment of new undertakings, mergers, amalgamations, takeovers, and the appointment of directors.

(c) The restriction of purchasing and transferring shares will be eliminated.

(d) The MRTP Commission will consolidate functions and be authorised to initiate investigations regarding monopolistic, restrictive, and unfair trade practices based on consumer complaints.

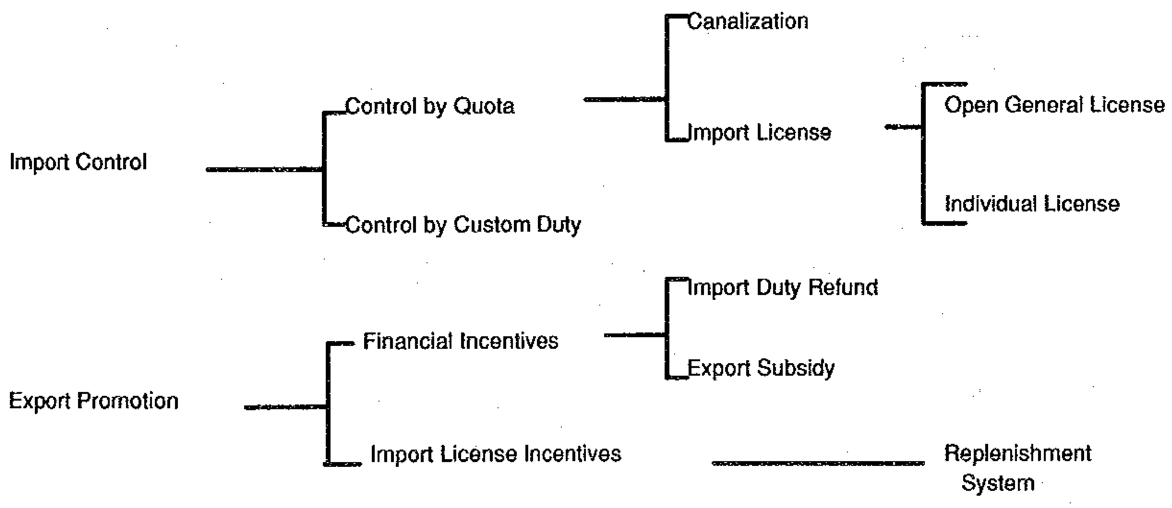
3.2 Trade Promotion Policy: Trends

3.2.1 Prior to the New EXIM Policy 1991

(1) Outline of the Import and Export Control Policy

(a) The basic external trade policy of India is "controlling imports and promoting exports" under a complete control system to counter the country's chronic trade deficit and shortage of foreign exchange reserves.

(b) The control system operated in two parts utilising the following measures:



(c) External trade is legally controlled by the "Import & Export Control Act, 1974", and various regulations announced under the Act.

(2) Outline of Previous Import Control Policy

(a) Controls utilising Quota:

i) Canalization (designated importers concentrating in the public sector)

The import and export of essential goods and bulky items (iron ore, manganese ore, salt, sugar, coal, petroleum oil and products, etc.) can be handled only by public sector organisations such as the STC and MMTC (a total of 16 organizations); the private sector is not allowed to participate.

ii) Import License System: Except for government imports and overseas aid, all imports are required to have an import license.

(b) Customs Duty Controls

In order to increase the central government's revenue, and to protect domestic industries, a majority of import items are levied import customs duty; the tariff of which is generally substantial.

(3) Outline of Previous Export Promotion Policy:

(a) Financial Incentives

i) Import Duty Refund

The import duty levied on the materials and components used for manufacturing export goods is refunded.

ii) Export Subsidy (Cash Compensation Support: CCS)

The government pays a cash subsidy (CCS) of 5.0 to 30.0 per cent of the export amount of such goods that the government encourages for exporting. This measure could have vitalized Indian exports, but at the same time it spurred a deficit that became a budgetary problem for the government.

(b) Import License Incentives

This is a Replenishment License system (REP), which permits exporters to import necessary materials and components used for manufacturing products for the export market. The license provides for companies to claim an amount of 5 to 20 per cent of the export FOB amount for those cases where similar domestic materials and components are not available; including pricing, quality and delivery of such items as exporters may deem as unsatisfactory for production.

3.2.2 The EXIM Policy 1991 (EXIM 91)

On 4th July 1991, the Minister of Commerce announced a new liberalised policy titled "Structural Change in the EXIM Policy", which attempts to significantly reform the previous export and import policies.

(1) The New Policy Objectives

The new EXIM policy objectives are as follows.

(a) Simplification of licensing, and encouraging liberalisation.
(b) Export promotion.
(c) Import compression to optimum level.

(2) New Policy: Subjects

The new policy as presented in the EXIM 91 are organised into the following 12 items:

(a) Replenishment system (REP license) was broadened and liberalised.

(b) REP Rates were enhanced and made uniform.

(c) Merger of additional licenses with REP licenses

(d) Suspension of Cash Compensatory Support (CCS).

(e) Licensing removed; most imports against REP only.

(f) Small scale industries, manufacturers of life saving drugs and equipment, REP licenses exempted.

(g) Strengthening of advance licensing as a measure of export promotion.

(h) Liberalising the trade of EXIM scrip (REP license)

(i) Financial institutions permitted to trade REP/EXIM scrip.

(j) Elimination of licenses within three years.

(k) De canalization of imports.

(l) Convertibility of Rupee within three to five years.

The items above can be classified into three broad areas: (1) simplification of the import licensing system; (2) increasing the import limit of the REP license; and (3) the abolishment of export subsidies. Details of the three classifications follow.

(3) Simplifying the Import Licensing System

(a) "Individual import license" was simplified, and imports of materials and components (except OGL items) used for manufacturing export products can be imported with a replenishment license (REP License).

(b) The imports of goods in the limited permissible list 3A, 3B, 4, 6, and 9, attached to "Import & Export Policy 90-93", can be imported with an REP License.

(c) "Supplementary License" is abolished and the REP License will be applied for all goods except for imports by the small scale industry, manufacturers of life saving drugs, and machines.

(d) All other import licenses acquired by exporters upto this time are replaced by the REP License.

(e) "Advance license" given to exporters for the import of materials and components for manufacturing export products without an import duty, is replaced by the REP License.

(f) When exporters plans to import simultaneously under the Advance License and REP License systems, exporters can obtain "Advance License". In this circumstance, the amount of the Advance License is increased to 20 per cent of the net foreign exchange earnings (NFE), instead of 10 per cent.

(g) The REP License in this new policy is called the "EXIM Scripps", and is freely traded.

(h) Elimination of licenses for capital goods and raw materials is projected by the government to occur in three years.

(i) The de canalization of imports will be achieved, shortly.

(4) Increasing the Import Limit of the REP License

(a) Previously, the REP License limit was 5.0 to 20.0 per cent of the export FOB amount. The New Policy increased the limit to 30 per cent uniformly, irrespective of the kind of export goods. The role of the REP License as an export promotion measure was substantially strengthened this time.

(b) Various licenses exporters previously received were abolished and canalised to the REP License as already stated. In relation to this reform, exporters will be given 5.0 per cent more in addition to the 30.0 per cent of export FOB amounts in the REP License.

(5) Abolishing Export Subsidy: Export subsidy was abolished as of July 3, 1991.

3.2.3 Import and Export Policy

The policy announced in March 1992, went into effect from April 1992 to March 1997 (same period as the Eighth Five Year Plan). Primary policy changes will liberalize imports of capital and intermediate goods for the manufacturing of export products. This policy is a significant change and demonstrates the governments strong intentions to liberalize the economy.

(1) The New Policy Objectives

The items which are not listed in the import negative list, can be imported freely. This policy promotes the "import free in principle", and "fewer restrictions, greater trade freedom, and less administrative controls".

The following eight objectives best describe the new policy.

(a) Preparing a foundation for the globalizing of Indian foreign trade.

(b) Increasing productivity, promoting modernization, and strengthening the competitive strength of India's domestic industries; reinforcing export competitive ability.

(c) Products improved to internationally acceptable quality and improve the image of Indian products abroad.

(d) Easing import procurement restrictions to reinforce export trade and the obtaining of raw materials, intermediate products, parts and accessories, and capital goods from the international market.

(e) The newly liberalized trade policy demonstrates efforts to develop import substitute products for the domestic market.

(f) Efforts to reduce and eliminate quantity restrictions, approval systems, and other regulations.

(g) Promoting research and development (R&D) to enhance development and the improvement of technology.

(h) Simplifying export and import procedures.

(2) Import Regulation Changes

(a) Negative List of imports was significantly reduced; three items were banned; 70 items subject to restriction; and eight items canalised.

(b) Consumer goods retained restrictions.

(c) Special import facilities for the hotel and tourism industry; and for sports groups.

(3) Export Regulation Changes

(a) The Negative list of exports was reduced to seven items banned, 62 items subject to restrictions, and 10 items canalised.

(b) The exporting of 46 items which required an export license permitted with minimum regulation (refer to the "Handbook of Export and Import Procedures, Part V").

(c) Capital goods imports for exporters are allowed at concessional custom duties rates. Import custom duty is reduced to 25 per cent of imported capital goods CIF value subject to three times the CIF value of exports for four years, and to 15 per cent of imported capital goods CIF value subject to four times the export amount for five years. (Note: the New Policy, Chapter 6, "Export Promotion Capital Goods Scheme.")

(4) Other Regulations' Changes

(a) Magnifying duty exemption scheme (refer to: New Policy, Chapter 7, "Duty Exemption Scheme").

(b) Export houses, trading houses, and star trading houses certificate holders can import goods for the purpose of export production under the duty exemption scheme (refer to New Policy, Chapter 7).

(c) Special favour was enlarged for the units operating in 100 per cent EOU, FTZ, and EPZ. Installment of mechanical equipment through leases (New Policy, Chapter 4, Article 96) and exports through exporters as mentioned in "b" above are permitted (New Policy, Chapter 4, Article 104).

(d) Deemed exports' transactions that relate indirectly to earning foreign exchange, are favoured with a duty exemption scheme and other benefits (refer to New Policy, Chapter 5).

(e) Capital goods were eliminated from the import negative list and may be imported with a license from the Export Promotion Capital Goods Scheme; used machines are also permitted for imports. (Refer to the New Policy, Chapter 6, EPCG, Article 40, and Chapter 5, Article 33.)

3.2.4 Amendments to the Foreign Exchange Regulations Act (FERA), 1973

The January 1993 amendments to the FERA are summarised and discussed below.

(1) Amendment objectives

(a) To further promote economic liberalisation efforts and strengthen new economic policies by legally enacting measures for thorough FERA enforcement, and ensure that India's efforts are understood by foreign countries.

(b) Abolishment of the "FERA Company" which identified a company as a foreign joint venture enterprise comprised of 40 per cent foreign held equity. Such companies were established under the Indian Company Act with an Indian joint venture partner, but were subject to governance as a 100 per cent foreign-owned enterprise. Abolishment of this distinction is considered favorable to foreign investors.

(c) FERA Company are treated the same as domestic companies. Specifically,

- Borrowing funds in India from resident Indians (Section 26).

- Appointment of an agent or technical or management adviser (Section 28).

- Acquisition of Indian companies, except agriculture and plantation fields (Section 29).

- Establishing branch or liaison office in India (Section 29).

- Acquisition and holding of immovable property in India (Section 31).

Although regulation of business activities was alleviated or abolished by notifications, companies with foreign capital experienced inconveniences due to misunderstandings by government service window representatives who were not properly notified of changes. This amendment provided a legal countermeasure for company's with foreign capital.

(2) Primary amendment subjects

(a) Restriction regarding assets held by non-residents (Section 11), deletion.

This section was introduced in the 1973 Act to provide statutory backing to the RBI's practice of blocking the securities of persons who had migrated abroad as well as to block the bank accounts and securities of prospective emigrants. The RBI no longer blocks such bank accounts. The accounts of such persons are treated as non-resident accounts on their becoming non-residents. Section 11 has now lost its relevance and is, therefore, deleted.

(b) Special accounts by which the central government can direct certain payments be made into a special account (Section 12, deletion).

Payments to specified areas from India can be made by opening a special account in the RBI or authorised foreign exchange dealers subject to the authority of the government. Deleted.

(c) Power of the Central Government to direct payment in foreign currency in certain cases (Section 15 deletion):

This section regulated payment by non-residents in foreign currency while on a visit to India. As the RBI has already granted general permission to firms, companies, or other organizations to offer hospitality to non-residents on visits to India, this section is deleted.

(d) Payment for exported goods (Section 18-A Addition):

A new Section 18-A was introduced that permits the taking out of goods on rental, lease, hire, or on any other arrangement which does not amount to the disposal of such goods.

(e) Transfer of Securities (Section 19, Amendment):

The provisions are 1) the transfer of any securities from a register in India to a register outside India, and 2) the transfer by a non-resident to another non-resident were deleted from this section. However, transfers by a non-resident to a resident and the transfer by a foreign national resident in India to another resident, both of which involve overseas remittances, are retained. In addition to shares, the transfer of debentures is regulated as well.

The transfer of any security from a register in India to a register outside India, is deleted under this section.

However, three types of transfer of shares were regulated - (a) transfer by a non-resident to another non-resident, (b) transfer by a non-resident to a resident, and (c) transfer by a foreign national resident in India to another resident. The question of share values and permission for remittances outside India, is retained.

(f) Holding of Securities (Section 21, deletion) . Following the deletion of Section 19 (1)-(a).

(g) Acquisition by the central government of foreign securities for puposes of strengthening the country's foreign exchange position (section 23, deletion).

(h) Restriction on the holding of immovable property outside India (Section 25, amendment):

This section was amended suitably to enable the RBI to grant general permission subject to certain conditions, as may be notified by the RBI from time to time.

(i) FERA companies and the Borrowing of Funds (Section 26, Amendment):

FERA Companies' borrowing restrictions regarding raising funds from a resident Indian and acquiring control, have been removed. However, the giving of a guarantee by an Indian resident in favour of an Indian non-resident is retained. Until recently, there were restrictions on FERA companies, but these restrictions are now abolished by deleting sub-sections (1) to (5), and sub-section (7) along with explanations (I), (II), and (III), under this section only sub-section (6) is retained which regulates the giving of guarantees by a person resident in India in respect of any debt or other obligation, or liability in favour of a person residing outside India.

(j) Restrictions on persons resident in India from participating in concerns outside India (Section 27, deletion). Resident Indians participating in joint venture works outside India, no longer require permission.

(k) Restrictions on appointment of certain persons and companies as agents or technical and management advisers in India (Section 28, Amendment).

It was decided to take FERA companies outside the purview of this section in regard to acceptance of appointment as an Agent or Technical or Management Adviser, or for the use of trade marks to which they were entitled. Therefore, restrictions under this section would henceforth, apply only to foreign companies, foreign citizens, and non-residents with regard to their acceptance of appointment as an Agent in India of any person or company.

(l) Restriction on establishment of places of business in India (Section 29, Amendment).

This section is amended exempting FERA companies from the prohibition imposed under Clause (a) and (b) of sub-section (1) on the establishment of a branch office or a liaison office even when the non-resident interest in such company exceeds 40 per cent. Such companies will also be allowed to acquire whole or part of any undertaking in India, of any person or company carrying on trade, commerce and industry, excepting agriculture and plantation activity. It is also clarified that restriction with regard to activities of companies registered outside India and foreigners would continue to be regulated under this section.

(m) Prior permission by foreign nationals before taking up employment in India (Section 30, amendment):

Because the RBI does not wish to regulate, this section has been amended accordingly. The Ministry of Home Affairs will, however, continue control through the granting of visas.

(n) Restriction on the acquisition, holding etc., of immovable property in India (Section 31 Amendment):

Henceforth, FERA companies do not need the RBI's permission for acquiring, holding, transferring or disposing of by sale, mortgage, deed, lease, gift, etc., any immovable property situated in India.

(o) Restrictions on overseas travel and travel-related business (Section 32, deletion)

Airlines and shipping companies, travel agents, etc., are no longer required to obtain a license from the RBI for arranging for transportation out of the country.

(p) Submission of returns and/or statements by authorized foreign exchange dealers (Section 73-A addition).

Penal regulations were strengthened against failures to report.

CHAPTER 4 THE FOREIGN INVESTMENT STRATEGY

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Specific legislative acts and regulations enacted in other developing countries to spur foreign investment are not identified in India. However, foreign and domestic investments are regulated by the "Industries, Development and Regulation Act, 1951", and subsequent "Industrial Policy", "Industrial Policy - Government Decisions" and "New Industrial Policy" announcements. Details regarding India's industrial and trade policies were introduced in Chapter 3, and relevant details of those policies with regard to foreign investment will appear here.

4.1 Foreign Investment Policy: A History

4.1.1 The Policies Prior to the "New Industrial Policy: 1991"

Beginning with the country's independence from England in 1947, the Government of India has adopted closed door policies to foreign investments in an effort to develop a self-sustaining, independent Indian economy. Further regulation of foreign investments were enacted with the passage of the Foreign Exchange Regulation Act (FERA) of 1973. The FERA is the only legislation that regulates foreign investments, and the main contents of the Act are:

(1) Foreign collaborations without technology transfers are not permissible in principle.

(2) Foreign equity shares cannot exceed 40 per cent in principle.

(3) Enterprises with more than 40 per cent foreign equity are termed "FERA Enterprises" and are more severely regulated than domestic companies.

In the 1980's, the central government decided that the promotion of foreign investments was essential for the revitalization of domestic industries, and that foreign investment restrictions should be gradually reduced. However, regulations imposing industrial licenses for new investments remained in effect until the announcement of "The New Industrial Policy, 1991" NIP-91). Important policies effecting foreign investments prior to the "NIP-91" are as follows:

August 1947	Independence; inauguration of Nehru Cabinet.

April 1948	Industrial Policy Resolution - 48, announced. (The government classifies the fields of the Public and Private sectors.)
October 1951	Industries, Development and Regulation Act - 1951, announced. (The government formulates a license system for new industries, expansion of existing industries, new production in existing industries, and removal of industries.)
April 1956	Industrial Policy Resolution - 56 announced. (The government reconfirms the construction of a "Socialist Pattern of Society". Existing private enterprises are not compulsory transferred to the public sector, but important, key industries are exclusively reserved for the public sector.)
December 1969	Monopolies and Restrictive Trade Practice Act (MRTP Act) issued. (Large scale enterprises regulated from expanding business activities.)
February 1973	Industrial Policy, Government Decisions announced. (The government introduces (1) the "Joint Sector", joint ventures between private and government-owned companies (primarily state-owned institutes), and (2) public financing institutes are able to convert partial credit amounts into equity shares of financed companies, formulating the Mandatory Convertibility Clause.)
September 1973	Foreign Exchange Regulation Act enacted. (Foreign investment restrictions institutionalised as legislation.)
November 1973	Secretariat of Industrial Approval (SIA) inaugurated. (SIA becomes the single window service for industrial license applications.)
October 1975	21 industries were liberalized from compulsive industrial licensing.

September 1977	100 joint-ventures officially requested to reduce foreign capital shares.
October 1977	50 joint ventures suspended from dividend remittances abroad. 25 foreign enterprises officially requested to end joint venture operations. (The government did demonstrate intentions to allow foreign collaborations only in the export-oriented or advanced technology industries.)
July 1980	The New Industrial Policy: 1980, announced. (Automatic approval procedures introduced to improve industrial productivity.)
April 1982	Industrial Policy Announcement. (Restrictions on the activities of MRTP and FERA enterprises partially eased, and industrial licensing simplified.)
January 1983	Technology Policy Announcement. (Initiatives for developing domestic industrial technologies, and invitation to gain foreign technology.)
December 1985	Industrial Policy Announcement. (Restrictions on MRTP and FERA enterprises operating in the backward territories, abolished.)

4.1.2 The New Industrial Policy, 1991

The New Industrial Policy announced in July 1991, abolished in principle industrial licenses with the exception of some industries. Domestic financial markets and entrepreneurs that were suspicious of the central government's industrial liberalization policies during the 1980's, were reported to have welcomed this new development. General business reports also demonstrated optimism in the government's ability to foster a continued and stable liberalization of the country's economic and industrial policies.

Significant topics regarding foreign investment policies are extracted and presented below in summary form.

(1) Automatic approval of foreign investments up to 51 per cent of foreign equity shares designated in the high priority industries (34 industries) were allowed through registration with the Reserve Bank of India.

(2) Applications for foreign investments of more than 51 per cent in the above industries were accepted by the Secretariat for Industrial Approvals (SIA), and timely decisions were forthcoming after complete consultation with the Foreign Investment Promotion Board (FIPB).

(3) Eighteen industries (including electrical white goods such as domestic refrigerators, domestic dish washing machines, programmable domestic washing machines, microwave ovens, air conditioners, and entertainment electronics such as video cassette recorders (VCRs), color televisions, compact disc (CD) players, tape recorders etc.), were requested to apply for industrial licenses regarding domestic investment. However, foreign investors were requested to only apply to the SIA for approvals (not for an industry license.)

(4) Automatic approvals for capital goods imports were issued in those cases where payments were to be made with a portion of the foreign participation.

(5) Foreign investments of less than 24 per cent in equity shares were approved for industries previously reserved for the domestic small- and medium-scale enterprises.

(6) The Phased Manufacturing Program (PMP) system was abolished for new industries.

(7) Dividend remittances abroad were classified as export earnings (termed "Dividend Balancing"), and were supervised by the Reserve Bank of India.

(8) Technical collaborations with foreign companies were automatically approved and royalty settlements were established as:

   (a) Fixed Royalty: below 10 million rupees.

   (b) Running Royalty: below 8 per cent of total sales. (domestic sales: 5 per cent).

(9) Export obligations were eliminated except for EOU and EPZ enterprises.

4.1.3 Policies Amended Subsequent to the " NIP-91"

Continuing the "NIP-91" liberalisation efforts, the Government of India announced several foreign investment amendments.

(1) Foreign Exchange Regulation Act Amendments.

(a) March 1992. (The statements of Minister of Finance)

Foreign exchange on trading account was allowed partial convertibility at free market rates, i.e., 60 per cent at market rates and 40 per cent at official fixed rates.
Exporters could earn foreign exchange rate advantages. Subsequently, the EXIM-SCRIP system mentioned in Chapter 3, was abolished.

(b) January 1993. (Presidential Ordinance)

The FERA enterprises (companies with more than 40 per cent of foreign equity) were considered equally with domestic companies and the following restrictions were abolished.

(i) Acquire financing from Indian residents.

(ii) Open branch offices or liaison offices in India.

(iii) To acquire Land.

(iv) Appointments as an agent or technical and management advisors in India.

(c) March 1993. (Minister of Finance's statement)

Full convertibility of trading accounts at the free market rate is implemented.

(2) The New Import and Export Policy (1992-97). (Announced March 1992)

To proceed with import and export liberalisation, the government adopted a policy that abolished licenses for external trade with a few exceptions listed in the "negative list". Thus, procedures for external trade were substantially altered and simplified.

(3) The Dividend Balancing System. (Press Note No.10 (30)92-UP, June 1992)

The Dividend Balancing System was abolished except for consumer goods manufacturers.

(4) Taxation. (Minister of Finance statement; March 1993)

(a) The Auxiliary custom duty was included with the Basic duty and the maximum custom duty was reduced to 85 per cent from the previous 110 per cent.

(b) Excise duties were reduced. (capital goods and equipment - 10 per cent from 11.5 to 23 per cent, automobiles - 40 per cent from 55 per cent.)

(5) Restricted industries. (The Special Committee statement of April 1993)

Motor cars, raw hides and skins, leather, and white goods (domestic refrigerators, domestic dish washing machines, programmable domestic washing machines, microwave ovens, air-conditioners) were eliminated from the List of Industries with respect to which industrial licensing will be compulsory.

4.2 The Statistical Record of Foreign Investment

4.2.1 The Foreign Investment Record

During the 1980's, gradual liberalization of India's industries proceeded. The average amount of foreign investment per annum for the five year period (1986 and 1990) totaled Rs. 1,789 million, about 2.4 times the average for 1981 and 1986 (Rs. 749 million). Given the exchange rate variances in the U.S. dollar to the Rupee for this period, foreign investment to India grew by an adjusted rate of 1.6 times during the latter half of the period. It should be noted that liberalisation policies regarding foreign investments were not effective during this period. (Refer to Table 4-1.)

The average foreign investment total per annum for 1991 and 1992, was Rs. 22,108 million, about 12.3 times the previous five years' average. Given the foreign exchange variances for this period, adjusted total per annum increased 6.6 times over the period prior to NIP-91 (See Table 4-2.)

In addition to the above, the four month record for January to April 1993, indicates a substantial positive trend (about twice that of the previous year) despite the recent sluggish world economy. (See Table 4-3.)

4.2.2 Country-Wise Foreign Investment Record

The Unites States indicated stronger investment interest, and ranked first among foreign investment to India. Investment from the United States increased as a per cent share of total foreign investments from 18 per cent in the first half of 1980's to 56 per cent in the first quarter of 1993 (1981 to 1985, 18 per cent; 1986 to 1990, 28 per cent; 1991 to 1992, 32 per cent; and January to April 1993, 56 per cent.).

Germany ranked second during the late 1980's, but recorded only a three per cent share of total foreign investment for 1991 and 1992, and only two per cent for the first quarter of 1993. The Chamber of Commerce and Industry of Germany reported that total foreign investment outlays in 1992 dropped 14 per cent from the previous year due to economic conditions, and anticipated foreign investments would primarily flow to European Community countries and to East European countries.

Japan recorded a 17 per cent share of total foreign investment to India during the first half of the 1980's, primarily in the automobile industry, but figures indicate only a five per cent share (ranked fifth) during the latter 1980's. Japanese total foreign investment to India for 1991 and 1992 represented a 15 per cent share, (investments primarily in the oil refinery and petro-chemical industries) and ranked third after the U.S. and Switzerland. During the first quarter of 1993, Japan ranked fourth in terms of total foreign investment to India (after the U.S., Thailand, and Switzerland).

Table 4-1 DIRECT FOREIGN INVESTMENT RECORD (1981 - 1990)

(unit: million rupees)

	81-85 Total	average (A)	(%)	86-90 Total	average (B)	(%)	B/A
USA	700.48	140.10	18.70	2,526.59	505.32	28.09	3.6
Germany	284.47	56.89	7.59	2,008.66	401.73	22.33	7.1
Japan	636.62	127.32	16.99	437.27	87.46	4.86	0.7
UK	170.87	35.37	4.72	726.03	145.21	8.07	4.1
Italy	128.91	25.79	3.44	469.00	93.80	5.21	3.6
France	75.68	15.14	2.02	365.19	73.04	4.06	4.8
Switzerland	-	-	-	-	*80.02	4.45	-
NRI	-	-	-	-	*144.09	8.01	-
others	1,749.15	349.33	46.54	2,461.26	820.42	14.92	-
Total	3,746.18	749.24	100.00	8,994.00	1,798.80	100.00	2.4

Remarks: (A) - 5 years (81-85) average per annum
(B) - 5 years (86-90) average per annum
* - 3 years (88-90) average per annum
Foreign Exchange Rate (81-85 average): US$1=Rs.10.08
Foreign Exchange Rate (86-90 average): US$1=Rs.14.96

Source: SIA

Table 4-2 DIRECT FOREIGN INVESTMENT APPROVAL RECORD (1991 - 1992)

(unit: million Rupees)

	91	92	Total	average(D)	(%)	C/A	C/B
USA	1,858.5	12,315.0	14,173.5	7,086.75	32.05	50.6	14.0
Germany	418.0	862.7	1,280.1	640.35	2.09	11.3	1.6
Japan	527.1	6,102.3	6,629.4	3,314.70	14.99	26.0	37.9
UK	321.0	1,176.7	1,497.7	748.85	3.39	21.0	5.2
Italy	178.1	893.9	1,072.0	536.00	2.42	20.8	5.7
France	192.3	296.4	488.7	244.35	1.11	16.1	3.3
Switzerland	355.0	6,817.6	7,712.6	3,586.30	16.22	-	44.8
NRI	197.0	4,391.3	4,588.3	2,294.15	10.38	-	15.92
others	1,294.1	5,719.5	7,314.2	3,656.80	16.54	-	-
Total	5,341.1	38,875.4	44,216.5	22,108.25	100.00	29.5	12.9

Remarks: (C) - 2 years (91-92) average per annum
: Foreign Exchange (91092 Average) - US$1=Rs.27.73
Source : SIA

Table 4-3 DIRECT FOREIGN INVESTMENT APPROVAL RECORD (January - April, 1993)

(unit: million Rupees)

	Jan.-Apr.	average (D)	%	D/C	D/B	D/A
USA	16,634.4	49,903.2	56.0	7.04	98.76	356.20
Germany	661.8	1,985.4	2.2	3.10	4.94	34.90
Japan	1,016.4	3,049.2	3.4	0.92	34.86	23.95
UK	653.7	1,961.1	2.2	2.62	13.51	55.45
Italy	310.3	930.9	1.0	1.74	9.92	36.10
France	54.7	164.1	0.3	0.67	2.25	10.84
Switzerland	3,573.6	10,720.8	12.0	2.99	133.98	-
NRI	1,910.2	5,730.6	6.4	2.50	39.77	-
Thailand	3,664.0	10,992.0	12.3	-	-	-
China	361.8	1,085.4	1.2	-	-	-
Singapore	354.0	1,062.0	1.2	-	-	-
Korea	24.6	73.8	0.1	-	-	-
Hong Kong	14.6	43.8	0.1	-	-	-
Taiwan	18.3	54.9	0.1	-	-	-
Others	457.6	1,372.8	1.5	-	-	-
Total	29,710.0	89,130.0	100.0	4.03	49.55	118.97

Remarks : (D) - Figure per annum averaged by 4 times of 4 months
Foreign Exchange Rate (Jan.-Apr average) - US$1=Rs.31.0
Source : SIA

4.2.3 Sector-wise Foreign Investments and Technical Collaborations

The foreign investment record during the post-liberalisation policy period (August 1991 to April 1993) for sector-wise foreign investments and technical collaborations, is presented in Table 4-4.

Fuel-related industries (electric power and petroleum-related enterprises) recorded a substantial share of foreign investments (47 per cent) for the period described. Electrical and general machines comprised 16 per cent; the food industries 13 per cent; and the chemical and fertilizer industries 9.0 per cent.

Records for the number of foreign investment (FI) and foreign technical collaborations (TC) applications indicate that the electrical and general machines industries ranked first (FI = 42 per cent; TC = 56 per cent), the chemical and fertilizer industries, second (FI = 13 per cent; TC = 4 per cent), the food industries ranked third (FI = 9 per cent; TC = 3 per cent), and the fuels industry ranked fourth, (FI = 2 per cent).

The countries with the largest shares of total foreign investments to India during the first quarter of 1993 invested in electric power generation (U.S. = Rs 15,838 million), shrimp feed mill, processed shrimp (Thailand = Rs. 3,660 million), and oil refinery industries (Switzerland = Rs. 2,660 million).

Table 4-4 Sector-wise Breakup of Foreign Investment and Technical Collaboration Approvals During Post Policy Period: August 1991 to April 1993

(Rs. in Million)

Sl. No. (1)	Name of the Industry (2)	Total (3)	Tech. (4)	Fin. (5)	Amount (6)	Percentage with total F.E. (7)
1.	Metallurgical Industries	115	74	41	1,211.15	1.67
2.	Fuels –					
	i) Power	6	-	6	17,393.15	23.92
	ii) Oil Refinery	12	2	10	16,172.32	22.24
	iii) Other	32	22	10	656.98	0.90
3.	Biolers & Steam Generating Plants	18	12	6	545.87	0.75
4.	Prime Movers (other than Elect. Generators)	-	-	-	-	-
5.	Electrical Equipment	461	263	198	5,026.42	6.91
6.	Telecommunication	57	37	20	1,337.00	1.84
7.	Transportation	132	94	38	1,714.40	2.36
8.	Industrial Machinery	345	254	91	1,216.88	1.67
9.	Machine Tools	34	21	13	79.87	0.10
10.	Agricultural Machinery	12	9	3	55.40	0.08
11.	Earth Moving Machinery	17	11	6	9.27	0.01
12.	Misc. Mechnical & Engg. Industry	105	65	40	390.08	0.54
13.	Commercial, Office & Household Equipment	27	16	11	673.18	0.93
14.	Medical & Surgical Appliances	15	5	10	48.85	0.07
15.	Industrial Instruments	50	32	18	167.26	0.23
16.	Scientific Instruments	21	7	14	345.35	0.47
17.	Mathematical, Surveying & Drawing Instruments	-	-	-	-	-
18.	Fertilizers	6	5	1	9.90	0.01
19.	Chemicals (Other than Fertilizers)	379	253	126	6,117.76	8.42
20.	Photographic Raw Film & Paper	4	3	1	79.00	0.11
21.	Dye stuffs	2	-	2	13.30	0.02
22.	Drugs & Pharmaceuticals	38	21	17	472.85	0.65
23.	Textile (including those dyes, printed or otherwise processed)	68	25	43	1,719.35	2.36
24.	Paper & Pulp including paper products	28	22	6	205.47	0.28
25.	Sugar	1	-	1	35.00	0.05
26.	Fermentation Inds.	13	5	8	639.85	0.88
27.	Food Processing Inds.	116	33	83	8,793.80	12.09
28.	Vegetable Oil & Vanaspati	11	2	9	126.25	0.17
29.	Soap, Cosmetics & Toilet preparations	6	3	3	191.13	0.26
30.	Rubber Goods	35	24	11	81.22	0.11
31.	Leather, Leather Goods and Pickers	28	8	20	337.15	0.46
32.	Glue & Gelatin	-	-	-	-	-
33.	Glass	18	13	5	510.69	0.70
34.	Cermics	54	21	33	447.48	0.62
35.	Cement & Gypsum products	16	10	6	188.20	0.26
36.	Timber Products	1	1	-	-	-
37.	Defence Industries	1	1	-	-	-
38.	Consultancy Services	59	24	35	165.45	0.23
39.	Service Sector	50	8	42	1,771.54	2.44
40.	Hotel & Tourism	26	8	18	2,159.19	2.97
41.	Trading Co.	50	-	50	108.05	0.15
42.	Misc. Industries	106	53	53	1,502.56	2.07
	TOTAL	2,575	1,467	1,108	72,718.62	100.00

Source : SIA

4.3 International Comparison of Investment Climate

Current worldwide circumstances are reducing foreign investments abroad, and India should recognise that the country is facing significant global competition, and must prepare the best possible investment climate to meet foreign investors' needs. Competing countries are currently providing innovative incentives and better investment environments to attract foreign investors.

Foreign investors consider a receptive investment climate demonstrates a candidate country's political and industrial policies are well integrated, and that global market conditions will allow for strategic shift in the flow of capital. Thus, the relative competitive position of India to attract foreign investment was compared to nine Asian countries: Pakistan, Sri Lanka, Bangladesh, Thailand, Malaysia, Indonesia, Philippines, China, and Vietnam.

4.3.1 Country Comparisons and Areas for Comparison

(1) Country comparisons

The rationale for country selections are as follows:

(a) Pakistan, Bangladesh, and Sri Lanka

Pakistan and Bangladesh border India, and have relatively large domestic markets and plentiful supplies of inexpensive labour. Sri Lanka is actively seeking foreign capital for export-oriented industries.

(b) Thailand and Malaysia

Compared due to each country's successful industrialization through the garnering of foreign investment.

(c) Indonesia and Philippines

Were selected for comparisons as each country is actively seeking foreign investments, and are expected to further strengthen industrial production in the near future.

(d) China and Vietnam

Included in the comparisons as each country has experienced rapid growth in foreign investment flowing into the country, and demonstrated foreign investors' interest during the past three years. For example, in the last half of 1990, China demonstrated an upward trend in foreign investment and reached a record in 1992. (US$14.5 billion in the first half of 1992, 3.2 times greater than for the same period the previous year.) Foreign investors' interests in Vietnam have increased and investments flowed into the country amounting to US$1.19 billion in 1991 (double the previous year levels).

Korea, Taiwan, and Singapore are not included in the comparisons as currently each country appears to not be actively seeking foreign investors.

(2) Areas for Comparison

The countries promoting foreign investments can be described based on geographical locations, size of domestic markets, labour force characteristics, social conditions, government industrialization policies, and the maturity of industrial development.

The following four factors are chosen for comparison purposes.

(a) Industrial Policy

Foreign investment policy is based on a country's industrial policy. Table 4-8 gives basic descriptions, i.e., regulated and /or priority fields of each country's industrial policy.

(b) Foreign Investment Policy

Table 4-9 provides descriptions, i.e., regulated/restricted and or priority fields of foreign investment to respective countries.

(c) Foreign Trade Policy

Foreign trade policies are important to foreign investors not only for importing capital equipment, main and sub materials, components, etc., but also for exporting the company's manufactured products. Table 4-10 describes foreign trade policy, including import duties and foreign exchange regulations.

(d) Foreign Investment Incentives

Policy statements and descriptions regarding foreign equity share, tax incentives, financial assistance, etc., are introduced in Table 4-11.

4.3.2 Comparison of Foreign Investment Climate

(1) Summary of Investment climate

Figure 4-1 indicates the Investment Relationships between Investor and Recipient Countries

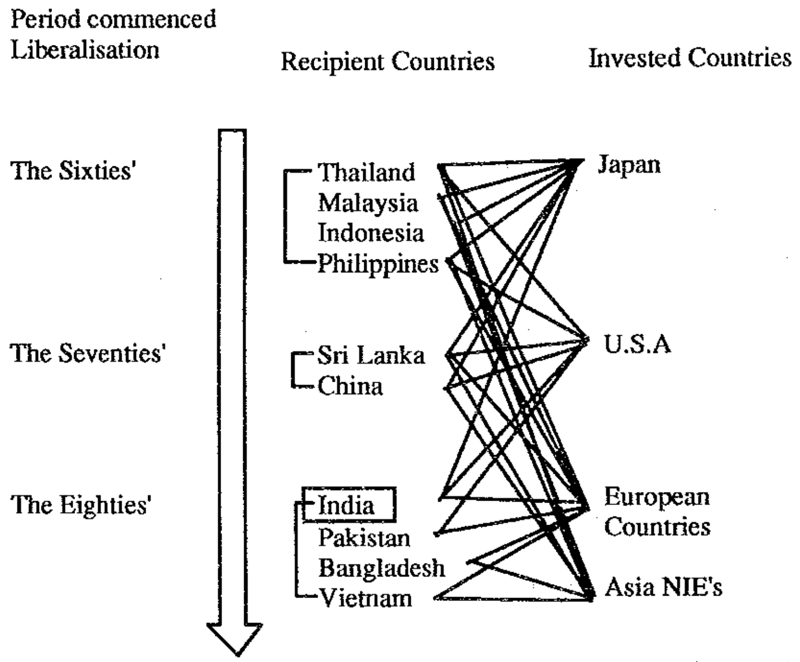

Figure 4-1 Investment Relationships between Investor and Recipient Countries

Characteristics of these foreign investments are as under:

(a) Direct foreign investments into ASEAN member countries began liberalization policies for foreign investments in the 1960's, and were concentrated initially in export-oriented industries. However, those trends have changed and there is an increase in domestic market oriented industries; especially internal trade in the Asian region.

(b) Direct foreign investments from the Asian NIE's countries have a significantly higher ratio following Japan and the U.S., and are expected to increase shares as these countries experience increased labour costs and labour relations problems. The NIEs are intending to shift production abroad.

(c) ASEAN member countries are also facing difficulties as labour shortages increase labour costs, lack of infrastructure such as electricity, tele-communications, and transportation, and the shifting of production to other countries.

(d) Countries that began foreign investment liberalization in the 1980's, including India, have received foreign investments from a few countries.

(e) Foreign investors previously hesitated to invest to China and Vietnam, due to the political situations in both countries, but are now demonstrating significant interest as each country's politics are demonstrating favorable climates for foreign investors. Both countries are in better geographical and historical positions than India when considering Japanese and Asian NIE's investors. China's potential domestic demand is significant (as is India's domestic market); both country's have inexpensive labour, and Vietnam's natural resources are as yet, to be fully developed. These conditions are attracting foreign investments.

(2) Investment Records Country-wise

Beginning in 1990, foreign investments have declined on a global basis, and investments to ASEAN member countries demonstrate similar trends as revealed in Table 4-5. Although, foreign investment to India, China, and Vietnam increased sharply for the same period (especially investments to China which ranked the highest in numbers of investors and invested amounts). The average amount invested per case for China, is comparatively low, while, India has a substantially higher level. It would appear that this discrepancy is due to the large scale of investments which flowed into the country.

Table 4-5 Country Records of Foreign Investments

(unit: US$ million)

	1998		1989		1990		1991		1992	
	No.	Amt.	No.	Amt.	No.	Amt.	No.	Amt.	No.	Amt.
India	962	172	605	195	666	73	951	235	1,002	1,001
Pakistan	NA	NA	NA	NA	NA	NA	NA	NA	NA	NA
Bangladesh	NA	3	NA	6	NA	53	NA	16	NA	19
Sri Lanka	N.A.	N.A.	39	28	40	68	79	193	205	357
Thailand	888	1,979	752	6,150	709	2,302	609	1,019	272	1,715
Malaysia	470	768	608	1,256	709	2,302	609	2,019	272	1,715
Indonesia	N.A.	4,409	N.A.	4,719	N.A.	8,705	N.A.	8,778	N.A.	4,702
Philippine	N.A.	473	N.A.	804	N.A.	961	N.A.	783	N.A.	155
China	5,954	5,297	5,779	5,600	7,273	6,596	12,973	11,977	13,069	14,533
Vietnam	37	360	69	512	108	589	150	1,185	113	1,995

Source: "Direct Foreign Investment from Japan and World". Japan External Trade Organisation

(3) Investment Climate Country-wise

Summary descriptions regarding investment circumstances are introduced and divided into the following three group:

Group (A) : Southwestern Asian Countries (Pakistan, Bangladesh, Sri Lanka)

Group (B) : ASEAN Countries (Thailand, Malaysia, Indonesia, Philippines)

Group (C) : Other Countries (China, Vietnam)

(a) Group (A)

Group (A) Countries border India and have similar geographical and historical conditions. Each country is liberalizing economic policies and is implementing deregulation measures and incentives to spur investments and the privatization of public sector industries. Also, these countries are emphasizing the promotion of exports, formulating Export Processing Zone(s) to attract foreign investors in order to earn foreign currency. Pakistan and Bangladesh are trying to establish industries in rural districts. Inexpensive and plentiful labour in these two countries attracts foreign investors, but unstable political situations, shortages of skilled labour, insufficient infrastructure, undeveloped domestic support industries, and inefficient administration continue to pose problems for foreign investors.

* Pakistan

Pakistan has adopted positive policies (as late as 1989) that include deregulation of foreign investment; especially, investment leading to the privatization of public sector industries. There are plans to establish a new EPZ and special industrial zone. From 1990, however, growth of new investment has stagnated. The slowing of investment to Pakistan is assumed to be related to the following conditions: global economic recessions, over-extended investments to prospective industries, insufficient infrastructure, unstable political and civil circumstances, inadequately trained work forces. Incentives are classified according to region and industry. Bio-technology, electronics, fertilizer, optical fiber, and solar energy are designated as key industries.

* Bangladesh

Bangladesh announced foreign investment promotion policies during the same period as Pakistan. Foreign investors were attracted to Bangladesh because of inexpensive labour , regulatory guidelines, and ordinances that protect investors' funds, etc. At the same time, Bangladesh was rendering negative images due to insufficient infrastructure and several natural disasters caused by cyclones and floods. Bangladesh's foreign investment record is dominated by innovators from the Asian NIE's and other ASEAN countries, primarily in the textile and garment industries. Foreign investment approval recorded a downward trend after reaching an investment peak in 1990. It should be noted that actual investment implementation has been comparatively lower than the approval records. The government announced a new industrial policy in 1991, and secured various incentives, including new systems for designating "The Special Economic Zone", and "The New EPZ". However, favorable results have not been observed.

* Sri Lanka

Sri Lanka began economic liberalization policies in 1977, earlier than Pakistan and Bangladesh, and has attracted foreign investors by establishing an "EPZ" and an "Investment Promotion Zone". In 1991, one hundred per cent foreign equity was automatically approved (except for some industries listed in Table 4-8). To simplify foreign investment application procedures, the government integrated foreign investment authorization agencies into the Board of Investment, which was strengthened and empowered to reinforce and enrich the various incentives for new investments. Sri Lanka is characterized by the small scale of its domestic economy, which forces the country to depend heavily on exports. Foreign investment was discouraged between 1983 and 1987, primarily because of civil disputes, but has recovered. Investors from Korea, Hong Kong, Japan, Germany, the U.K., and the U.S. have established business relationships in Sri Lanka. Foreign investment has flowed to many kinds of industries, but especially to labour intensive textile and garment industries, and capital intensive metal products and machinery industries (in addition to the electric and electronic high technology industries). Rapid increase in investment to the country is primarily due to government actions that promoted better investment policies, significant incentives, and the availability of a work force.

(b) Group (B)

Direct foreign investment to Group (B) countries began during the 1960's. The initial industrialization policies of these countries were for import substitution, but after the 1970's, policies changed and encouraged the promotion of export-oriented industries. Consequently, ASEAN countries demonstrated significant economic growth due to a manufacturing base that exported to Japan, the U.S., and Europe. Recently, the Asia Free Trade Association (AFTA) has formed an Asian economic bloc that includes ASEAN Countries and Asian NIE's, and has accelerated the region's economic stability and growth. Direct investments to ASEAN countries demonstrated rapid growth in the 1980's, and slowed after 1991. Primary reasons for the slowing in investments was believed to be due to increased labour costs, shortage of skilled workers, infrastructure inadequacy, lack of suitable industrial lands, inflationary trends, and the slowing of economies in the investor countries. As described in Table 4-7 and 4-8, governments are responsible for defining industrial sectors by utilising assistance and incentives. To promote investments, countries are establishing "Single Window Service" agencies for investors.

* Thailand

The number of applications for foreign investment to Thailand began to decrease after peaking in 1988. External factors effecting investment were deterioration of economic conditions in investor countries like Japan and the U.S., and increases in competition between neighbouring countries for foreign investment funds. Domestic factors related to regional gaps in economic expansions by these countries, due to concentrated investment in metropolitan areas, the ecological deterioration, and infrastructure inadequacy. And, fundamentally, unbalanced industrial structures which are observed as poorly developed domestic support industries. Given these circumstances, Thailand continues to attract substantial foreign investments as the country's investment climate provides simplified application procedures, and incentives targeted to selected industries. To encourage dispersion of industries into rural districts, the government has divided the country into three zones. Zone 1 covers the metropolitan districts in which investment is not promoted. In Zone 2, which surrounds Zone 1 and Zone 3, promotion is primarily targeted at investments, and the government provides individual incentives and promotion policies. The government also provides specific incentives for EPZ(s) and Special Industrial Zone(s), as well as for government-designated special industries.

* Malaysia

Among ASEAN countries, Malaysia has achieved the second highest growth compared to Asian NIE's. As for industrial fields in the 1990's, investments in the electric and electronic industries, basic metal products, and petroleum-related industries, were substantial. Foreign investment targeted the export-oriented manufacturing industries, but, as a result of sharp economic growth, worker shortages, immature medium/small-scale businesses, belated development of human resources and technology, etc., surfaced. Under these circumstances, the government revised its approach to foreign capital to attract investment in capital/technology-intensive industries to promote a more sophisticated domestic industry structure. The tax incentives for industries located in Free Zone(s) and bonded factories, are still effective. The government is providing favorable incentives for industries that contribute to the development of the Malaysian economy by designating the promotion of exports in pioneer industry.

* Indonesia

Indonesia is characterized by a strong nationalism that closed economic policies after gaining independence compared to other ASEAN countries. Throughout the 1960's, foreign private capital investments in the country accounted for only two per cent of total public investment, demonstrating negative foreign capital investment policies. As the Indonesian economy depended on primary resources such as petroleum, rubber, and tin, the country was significantly effected by international market prices. As a result, the country emphasized development of export-oriented and labour-intensive industries during the Fifth 5 year Plan (1989 to 1993), and implemented positive deregulation to attract foreign investors. Substantial growth of investment into the country was observed during the last five years of the 1980's. Beginning in 1992, however, foreign investment diminished sharply because of a shift of investment from Korea and Taiwan, to China. Also, Indonesia experienced an economic slump and investments decreased from Japanese investors. In Indonesia, enterprises are divided into two classifications: the PMDN (domestic capital only) and PDM (with foreign capital participation), and are regulated by respective activities. Foreign investment policies are severe compared to other ASEAN countries, with regulations as to the upper limits of foreign equity, and obligations to reduce foreign equity ratios within designated periods. In addition to the above, complicated administrative guidance obstructs the promotion of foreign investments. Although Indonesia has the largest population in Southeast Asia, and the largest scale of potential markets, the growth of foreign investment into this country remains stagnant. The government is planning gradual deregulation of investments. Currently, Indonesia has not proposed any taxation incentives.

* Philippines

The amount of foreign investment to the Philippines is the least among the four ASEAN countries previously described. Primarily, a lack of investment is linked to unstable political situations, and substantial infrastructure problems, especially in the area of power supply. The government enacted in 1991, the Foreign Investment Law, and approved 100 per cent foreign equity holdings except for designated industries.

Limited for three years, domestic market-oriented industries were also granted 100 per cent foreign equity. The government has plans for various incentives, deregulation of foreign exchange, and for the development of infrastructure.

(c) Group (C)

China and Vietnam are attracting foreign investors. China has as large a domestic market as India. Vietnam is a late-comer to the field of foreign investment, and foreign investors are considering the country's untapped resources and inexpensive labour force.

* China

In 978, China began an open foreign investment policy. In the initial stage of liberalization, 1978 to 1982, investment was primarily through official assistance from foreign countries, however, recent direct investments in the private sector have increased. Some factors associated with this are: (1) a large domestic market, (2) plentiful and inexpensive labour supply, (3) available and inexpensive raw materials. China's relatively late liberalization, however, seems to bring difficulties pointed out by the foreign investor, and are listed as follows:

i) Hierarchical administrative organizations require complex, bureaucratic procedures that deter investors seeking timely decisions regarding investment proposals.

ii) Requests related to Balance of Payments issues are severe.

iii) Infrastructure such as power, water supplies, sewerage, transportation, port facilities, and communication networks are not fully developed.

iv) Perception gaps regarding contractual obligations.

v) Support industries are inadequately developed.

vi) Difficulties associated with procuring stable raw material supplies.

vii) Business rules and regulations are not properly enacted.