The price situation during the Seventh Plan (1985-90) called for great caution due to 17.4 per cent per annum increase in M_3. The RBI tried to meet the challenge adequately by not only raising the CRR to 15 per cent and SLR to 38 per cent, but also by reducing refinance facilities drastically. Inflationary pressure nonetheless further increased in 1990-91 and to counteract it the SLR was raised to 38.5 per cent. The bank rate was raised to 11 per cent on July 4, 1991 and further to 12 per cent on October 8, 1991. The current rate of inflation does not warrant any complacency but the government no longer favours reliance on the SLR and the CRR to check it. Hence, these have been brought down in a phased manner. ***The effective SLR on total outstanding net demand and time liabilities has been brought down to 25 per cent.*** The CRR which is the only effective instrument of monetary control in India is being no longer depended upon to combat inflation. ***It was lowered down to 4.5 per cent on June 14, 2003.*** The objective of RBI's policy is to reduce CRR to statutory minimum of 3 per cent. Nevertheless, in order to check liquidity overhang the RBI raised CRR to 5 per cent effective from September 11, 2004. It was raised further to 7.5 per cent on November 10, 2007. ***The bank rate has also been brought down to 6.0 per cent.*** These are significant developments and must be taken into consideration by the RBI while the supply of money is expanded.

During the fifteen year period from April 1, 1991 to March 31, 2006 the quantities of M_1 and M_3 expanded at the annual rates of 15.7 and 16.8 per cent respectively. Obviously ***these rates of monetary expansion are unsustainable in the long run.*** The government and the RBI, however, failed to draw any lessons from the past. In these years bank credit to corporates registered a substantial increase despite lacklustre economic growth. This approach is likely to create inflationary pressures. The government must recognise the fact that monetary policy is a prime instrument in controlling inflation. In this context Vijay Joshi and I.M.D. Little rightly assert that ***"a low trend rate of inflation requires firm control of the rate of monetary expansion."***[28]

From the foregoing review of the monetary policy of the RBI it is not difficult to note that the government in the past has not allowed the RBI to impose drastic controls for containing inflation probably because of the apprehension that it could adversely affect the economy's growth performance. According to C. Rangarajan, over the years the following three factors have essentially guided the conduct of the monetary policy. "First, monetary policy measures have generally been a response to fiscal policy. This is particularly noticeable since the early 1970s when a sizable increase in RBI credit became a normal feature...Secondly, while monetary policy has been primarily acting through availability of credit, the cost of credit has also been adjusted upwards some time very sharply to meet effectively the inflationary situations...Thirdly, the areas of operation of monetary policy did not remain confined to those related to regulation of money supply and keeping prices in check. A more direct involvement of the monetary authority in the allocation of credit to the non-government sector became an important element of national economic policy, especially after the nationalisation of major banks in July 1969.[29]

Since the introduction of the economic reforms in 1991, the lowering of the CRR and SLR and the reduction in the bank rate clearly suggest that the entire concern of the monetary policy in the post-reform period has been to ensure adequate expansion in credit to assist industrial growth. Maintenance of a reasonable degree of price stability is relevant only to the extent it helps in achieving a faster rate of industrial growth.

The RBI now asserts that monetary policy over the years has emerged as a potent instrument of economic management. In its *Report on Currency and Finance 2003-04* the RBI states, "It is now widely agreed that monetary policy can contribute to sustainable economic growth by maintaining low and stable inflation. Within this overall objective of price stability, central banks attempt to stabilise output around its potential. In order to create enabling conditions for low and stable inflation as well as inflation expectations, there is an emerging consensus to secure the independence of monetary policy from the budgetary requirements of the base."[30]

The *Report on Currency and Finance 2003-04* further says, "While financial and external liberalisation present opportunities, they also throw challenges for policy authorities. Monetary authorities are increasingly required to take cognisance of not only domestic shocks but also external shocks. Given their objectives, central banks are required to mointor various segments of financial markets to ensure orderly conditions."[31]

From these observations of the RBI, it is obvious that it exaggerates the role of the monetary policy *vis-a-vis* the fiscal policy. Moreover, while emphasising price stability, it tries to obliterate the importance of employment generation for human well-being. This approach of the RBI is definitely influenced by the theoretical framework developed by the conservative monetary economists of the Chicago school.

According to Partha Sen, monetary policy has a limited role in the Indian context. He states, ***"Monetary policy in India is functioning in an environment where it can be expected to deliver very little if anything at all. At the best of times monetary policy can ensure a smooth functioning of an economy if a number of***

***pre-conditions are met. Put differently, monetary policy in India can do a lot of damage but its ability to singlehandedly do good is limited.*"**[32]

NOTES

1. Govenment of India, Planning Commission, *Seventh Five Year Plan* 1985-90, Vol. I (Delhi, 1985) p. 68.
2. C. Rangarajan, *Indian Economy: Essays on Money and Finance* (New Delhi, UBS Publishers' Distributors Ltd. 1998) p. 6.
3. Editorial, "A Beginning but Miles to Go," *Economic and Political Weekly*, February 15, 2003, p. 580.
4. Arun Kumar, "Changing Colours: How Black Turns into White," *Sunday Times of India (New Delhi)*, March 13, 2005, p.10.
5. H.H. Hinrichs, *A General Theory of Tax Structure Change during Economic Development* (Cambridge, Mass., 1966).
6. R.J. Chelliah, "Changes in Tax Revenue Structure — A Case Study of India" (Paper presented at the 42nd Congress of International Institute of Public Finance, Athens, August 1986).
7. R.J. Chelliah and R.N. Lal, *Incidence of Indirect Taxation in India 1973-74* (New Delhi, 1981).
8. E. Ahmad and N. Stern, "Effective Taxes and Tax Reform in India" (University of Warwick, Development Economics Research Centre, Discussion Paper No. 25, January 1983).
9. Raja J. Chelliah, *Towards Sustainable Growth: Essays in Fiscal and Financial Sector Reforms in India* (Delhi, 1996) p. 50.
10. Raja J. Chelliah, "Growth of Indian Public Debt" in Bimal Jalan (ed.), *The Indian Economy — Problems and Prospects* (New Delhi, 1992), PP. 219-20.
11. *Ibid.*, p. 219-220.
12. Shankar Acharya, "India's Fiscal Policy," in Robert Lucas and Gustav F. Papanek (eds.), *The Indian Economy - Recent Development and Future Prospects* (Delhi, 1988), p. 294.
13. Amiya Kumar Bagchi, "Neo-Liberal Reforms with Cosmetic Changes?" *Economic and Political Weekly*, August 7, 2004, p. 3574.
14. Ajit Karnik, "Fiscal Responsibility and Budget Management Bill —Offering Creditable Commitments," *Economic and Political Weekly.* January 19, 2002 p. 302.
15. Mihir Rakshit "Restoring Fiscal Balance through Legislative Fiat —The Indian Experiment", *Economic and Political Weekly.* June 9, 2001, p. 2061.
16. *Ibid.*, p. 2061.
17. Prabhat Patnaik, "A Tactical Compromise," *Frontline*, March 25, 2005, p. 35.
18. C.P. Chandrasekhar and Jayati Ghosh, *The Market that Failed — A Decade of Neo-Liberal Economic Reforms in India* (New Delhi. 2002), p. 84.
19. Surajit Das, "Effect of Fiscal Deficit on Real Interest Rates," *Economic and Political Weekly,* March 20, 2004, p.1310.
20. C.P. Chandrasekhar and Jayati Ghosh (2002), *op.cit.*, p. 86
21. S.L.N. Simha, *Essays on Finance* (Bombay, 1967) p. 35.
22. Y. Venugopal Reddy, *Monetary and Financial Sector Reforms,* (New Delhi, 2000), p.64.
23. Quoted in Andrew Crockett, "Central Banking jn the New Millennium", in Montek S. Ahluwalia. Y.V. Reddy and S.S. Tarapore (eds.), *Macroeconomics and Monetary Policy* (New Delhi, 2002), p. 132.
24. The concept of broad money is as follows:
    M_3 Multiplier = M_3 + RM
    where M_3 is broad money
    RM is reserve money
25. B. Rama Rao, *Evolution of Central Banking in India* (Bombay, 1960), p. 49.
26. H.V.R. Iyengar, *Monetary Policy and Economic Growth* (Bombay, 1962), p. 195.
27. Suraj B. Gupta, *Monetary Planning for India* (Delhi: Oxford University Press, 1981), p. 141.
28. Vijay Joshi and I.M.D. Little, *India's Economic Reforms* 1991-2001 (Delhi, 1996), p. 46.
29. C. Rangarajan, "Issues in Monetary Policy" in P.R. Brahmananda and V.R. Panchamukhi (eds.). *The Development Process of the Indian Economy* (Bombay, 1987), pp. 839-40.
30. Reserve Bank of India, *Report on Currency and Finance 2003-04* (Mumbai, 2004) p. 28.
31. *Ibid.* p. 79.
32. Partha Sen, "An Exercise in Fire Fighting", *The Economic Times* (New Delhi), October 31, 1998.

CHAPTER

27 INDUSTRIAL POLICY

Industrial Policy Resolution of 1948
Industrial Policy Resolution of 1956
• Salient Features of the Industrial Policy of 1956
Amendments in Industrial Policy of 1956
• Industrial Policy Developments in 1980s
New Industrial Policy, 1991
• Abolition of Industrial Licensing • Public Sector's Role Diluted • MRTP Limit Goes • Freer Entry to Foreign Investment and Technology • Other Liberalisation Measures
Appraisal of New Industrial Policy

When India became Independent in 1947, the industrial base of the economy was very small and the industries were beset with many problems such as shortage of raw materials, deficiency of capital, bad industrial relations, etc. The investors were not sure about the industrial policy of the new national government and the industrial (and investment) climate was wrought with uncertainties and suspicions. The government thus called an Industrial Conference in December 1947 to improve matters and remove the uncertainties and suspicions in the minds of investors and entrepreneurs. The Conference adopted a resolution for industrial peace and recommended a clear-cut division of industries into the public sector and private sector.

In this chapter, we propose to discuss the following questions :

What was the industrial policy in the pre-liberalisation phase (i.e. the pre-1991 period) ? We shall divide this discussion into three parts — Industrial Policy Resolution of 1948, Industrial Policy Resolution of 1956 and Amendments in Industrial Policy of 1956).

What are the features of the new industrial policy, 1991? (After describing the features we also present a critical appraisal of this policy).

INDUSTRIAL POLICY RESOLUTION OF 1948

The first important industrial policy resolution was issued by the Government of India on April 6, 1948. Following were the main features of the 1948 industrial policy:

1. Acceptance of the importance of both private and public sectors. The industrial policy resolution accepted the importance of both public and private sectors in the industrial economy of India. It assigned a progressively active role to the State but expressed the view that, "the mechanism and resources of the State may not permit it to function forthwith in industry as widely as may be desirable." Consequently the Resolution adopted a two-pronged strategy—(*i*) expansion of the State sector in areas where it was operating and in new lines of production, and (*ii*) allowing the private sector to subsist and expand albeit under proper direction and regulation.

2. Division of the industrial sector. The Resolution divided industries into four categories thereby putting to end all speculation and suspicion in this regard. These categories were as under: (*i*) ***Industries where***

State had a monopoly: In this category *three* fields of activity were specified—arms and ammunition, atomic energy and rail transport. (*ii*) ***Mixed sector***: In this category, the following six industries were specified—coal, iron and steel, aircraft manufacture, ship building, manufacture of telephone, telegraph and wireless apparatus (excluding radio sets) and mineral oils. "Except where, in the national interest, the State itself finds it necessary to secure the cooperation of private enterprise", the State was to have exclusive right to the setting up of new undertakings in this category. However, existing private undertakings in this field were allowed to continue for ten years after which the government would review the situation and acquire any existing undertaking after paying compensation on a "fair and equitable basis". (*iii*) ***The field of government control:*** 18 industries of national importance were included in this category. The government did not undertake the responsibility of developing these industries but considered them of such importance that their regulation and direction was necessary. Some of the industries included were—automobiles, heavy chemicals, heavy machines, machine tools, fertilizers, electrical engineering, sugar, paper, cement, cotton and woollen textiles. (*iv*) ***The field of private enterprise:*** all other industries (not included in the above three categories) were left open to the private sector. However, the State could take over any industry in this sector also if its progress was unsatisfactory.

3. Role of small and cottage industries. The 1948 Resolution accepted the importance of small and cottage industries in industrial development. These industries are particularly suited for the utilization of local resources and for creation of employment opportunities. However, they have had to face acute problems of raw material, capital, skilled labour, marketing etc. since a long period of time. Accordingly, emphasis was laid in the industrial policy that these problems of small-scale and cottage industries should be solved by the Central government with the cooperation of State governments.

4. Other important features of the industrial policy. The role of foreign capital in industrial development of the economy was recognized but the need of regulating and controlling it according to the needs of the domestic economy was deemed essential. Therefore, it was stated that in those industries where foreign investment was to be done, Indians should have a major say in the ownership and management. The Resolution called for harmonious relations between the management and labour since this was necessary for industrial development. For this purpose, the Resolution enunciated a policy of just labour conditions wherein workers would be given fair wages. For purposes of maintaining industrial peace, labour participation in management was also stressed.

Indian capitalists were satisfied with the Industrial Policy Resolution of 1948 since the role assigned to the public sector in that policy was, on the whole, acceptable to them. However, there were certain weaknesses and gaps in the 1948 policy and it was subjected to a number of criticisms.

INDUSTRIAL POLICY RESOLUTION OF 1956

The 1948 policy remained in vogue for full eight years and determined the nature and pattern of industrial development in the country. This period was marked by some significant changes in the economy. The country had completed one five year plan in the period 1951-56. Industries (Development and Regulation) Act, was passed in 1951[1] and gave the government the necessary experience and expertise in regulating and controlling industries in the private sector. The ruling party had declared 'socialist pattern of society' as the goal for the country. Because of these factors, a new declaration of industrial policy seemed essential. This came in the form of Industrial Policy Resolution of 1956.

The 1956 Resolution laid down the following objectives for the industrial policy: (*i*) to accelerate the rate of growth and to speed up industrialization; (*ii*) to develop heavy industries and machine making industries; (*iii*) to expand public sector; (*iv*) to reduce disparities in income and wealth; (*v*) to build up a large and growing cooperative sector; and (*vi*) to prevent monopolies and the concentration of wealth and income in the hands of a small number of individuals.

These objectives, it was thought, would help in generating more employment opportunities and in raising the standard of living of the masses. For this purpose, stress was laid on cooperation between public and private sectors but an increasing role was envisaged for the former so that, in due course of time, it could gain 'commanding heights' of the economy.

Salient Features of the Industrial Policy of 1956

Division of the industrial sector. As against four categories in the 1948 Resolution, the 1956 Resolution divided industries into the following three categories:

(a) ***Monopoly of the State.*** In the first category, those industries were included whose future development would be the exclusive responsibility of the State. Seventeen industries were included in this category and were listed in Schedule A (appended to the Resolution). These industries can be grouped into the following five classes: (*i*) defence industries, (*ii*) heavy industries, (*iii*) minerals, (*iv*) transport and communications, and (*v*) power. Of these, four industries—arms and ammunition, atomic energy, railways and air transport, were to be the government monopolies. In the remaining 13 industries, all new units were to be established by the State. However, existing units in the private sector were allowed to subsist and expand. The State could also elicit the cooperation of private sector in establishing new units in these industries 'when the national interest so required'.

(b) ***Mixed sector of public and private enterprise.*** In this section 12 industries listed in Schedule B (appended to the Resolution) were included. These were: all other minerals (except minor minerals), road transport, sea transport, machine tools, ferro-alloys and tool steels, basic and intermediate products required by chemical industries such as manufacture of drugs, dyestuffs and plastics, antibiotics and other essential drugs, fertilizers, synthetic rubber, chemical pulp, carbonization of coal, and aluminium and other non-ferrous metals not included in the first category. In these industries, State would increasingly establish new units and increase its participation but would not deny the private sector opportunities to set up units or expand existing units.

(c) ***Industries left for private sector.*** All industries not listed in schedules 'A' or 'B' were included in the third category. These industries were left open to the private sector. Their development was to depend on the initiative and enterprise of the private sector, though even here the State could start any industry in which it was interested. However, the main role of the State in this category was to provide facilities to the private sector to develop itself.

Mutual dependence of public and private sectors. The public and private sectors were not to be exclusive and totally independent of one another. The government could establish units in any of the industries (included in any category) on the one hand and could also allow the private sector to operate in any field reserved for the public sector. The only four industries in which private sector was not allowed to function were arms and ammunition, atomic energy, railway and air transport. In all other industries either the private sector was allowed to operate freely or its help could be obtained if the government deemed fit. Accordingly, the 1956 Resolution emphasized not only the mutual coexistence of private and public sectors but also provided for their mutual cooperation and help.

Assistance and control of private sector. According to the 1956 Resolution, the government could assist expansion and development of private sector through participation in its risk capital and share capital and by providing other types of services, fiscal incentives etc. However, the private sector was also to fit into the "framework of the economic and social policy of the State". Thus, the private sector was to remain subject to various government regulations and controls. Such regulation and control was to be exercised by the government through the Industries (Development and Regulation) Act, 1951, and other related legislations.

Importance of small-scale and cottage industries. The 1956 Resolution recognized the importance of small-scale and cottage industries just as the 1948 Resolution had done. Such industries could create large scale employment opportunities, ensure a more equitable distribution of income and wealth, and help in effective mobilization of human and physical capital. Assistance to this sector was to be provided either through direct means or through indirect means.

Reduction of regional inequalities. The 1956 Resolution called for reduction in regional imbalances and inequalities. For this purpose it was advocated that transport facilities, power and other facilities should be provided in the backward regions. Stress on balanced development of agriculture and industry in each region was also laid.

As compared to the 1948 Resolution, the 1956 Resolution considerably enlarged the area of operation of the public sector as the exclusive responsibility of the State was enlarged from 6 to 17 industries (Schedule A). In addition, another category including 12 industries (Schedule B) was defined where the State could participate on an increasing scale. However, the 1956 Resolution dropped the 'threat' of nationalization that the 1948 Resolution contained and the division of industries in different categories was more flexible in the former as compared to the latter. The fact is that the basic objective of both the Resolution was the same—strengthening the mixed economy structure of the country.

According to Jagdish Bhagwati and Padma Desai, "The second I.P.R. despite its close similarity to the first appears to have been issued partly to re-emphasize the importance of the public sector and the necessity to regulate the growth of the private sector in the light of the shift to a more explicitly 'socialistic' stance by

the government".[2] Nehru was particularly enthusiastic about the role of such policy in the evolution of a 'socialist' society. Accordingly, it was natural for him to emphasize the role of the public sector through the 1956 Resolution.

AMENDMENTS IN INDUSTRIAL POLICY OF 1956

The Government of India adopted a new Industrial Policy Statement on February 2, 1973. Though the basic structure of 1956 Resolution was kept intact, yet the Policy Statement of 1973 gave considerable concessions to private sector units and foreign multinationals. The government prepared a list of 19 industries whose development was of fundamental importance to the country. This list included "the core industries of importance to the national economy in the future, industries having direct linkages with such core industries, and industries with a long-term export potential." This list was put in Appendix I of the Industrial Policy Statement and has come to be known as the "Appendix I list". Industries in this list were opened to the MRTP and FERA companies provided the concerned items of manufacture are not specially reserved for the small-scale or public sectors. The Appendix I list mainly consisted not only of the basic, large-investment and complex-technology industries but also others the reason for whose inclusion in the list remains unclear. For example, a general term "scientific instruments" was included; so also "synthetic detergents". The list was modified and added to in later years with a view to including things which had become important over time (for example, alternate energy systems, turbines, optic fibre, energy efficient lamps, industrial laminates, personal transport vehicles, etc.)

Another important Industrial Policy Statement was announced by the government on July 23, 1980. Its objective was defined as facilitating an increase in industrial production through optimum utilization of installed capacity and expansion of industries. It emphasized rapid and balanced industrialization of the country with a view to benefiting the common man by increasing availability of goods at reasonable prices, larger employment and higher per capita incomes. The major function laid down by the new Policy Statement was solving the problem of shortages of major industrial inputs like energy, transport and coal.

The 1980 Statement extended the provision of automatic growth to more industries. Special steps were initiated to increase earnings from exports (for instance, exemptions from the locational policy, allowing duty free imports of capital goods, raw materials and components, etc). Also, recognition of actually installed capacity was permitted for the entire list of industries included in Appendix I of the Industrial Policy Statement of February 2, 1973, as also to other 15 industries, some of which produce items of mass consumption. In order to promote the growth of small-scale industries, investment limit for small-scale sector was raised from Rs. 10 lakh to Rs. 20 lakh. Similarly, investment limit for ancillary units was increased from Rs. 15 lakh to Rs. 25 lakh. Installed capacities in excess of licensed/registered capacities in 34 selected industries were regularised. These included basic industries and those producing mass consumption goods not reserved for the small sector, provided the firms were not units to which the Monopolies and Restrictive Trade Practices Act, 1969, or the Foreign Exchange Regulation Act, 1973, applied. Subject to similar qualifications, automatic growth was allowed to the extent of 5 per cent per annum or 25 per cent in a five-year period in registered or licensed capacity of 19 additional industries bringing the total of such industries to 34.

Industrial Policy Developments in 1980s

The decade of 1980s witnessed several steps to liberalise the industrial policy as the following discussion clearly brings out:

Exemption from Licensing. The limit of exemption from licensing was continuously raised upwards. In March 1978 the limit was fixed at Rs. 3 crore. During 1980s it was first raised to Rs. 5 crore in 1983 and then to a whopping Rs. 15 crore for projects located in non-backward areas and Rs. 50 crore for projects located in backward areas in 1988-89 (under certain conditions).

Relaxations to MRTP and FERA Companies. Under the pretext of expanding industrial production and promoting exports, various concessions were provided to companies failing under the MRTP Act (Monopolies and Restrictive Trade Practices Act) and FERA (Foreign Exchange Regulation Act). The most important relaxation related to the raising of the limit for MRTP companies from Rs. 20 crore to Rs. 100 crore (*i.e.* by five times) at one stroke in March 1985. On December 24, 1985, the government permitted the unrestricted entry of large industrial houses and companies governed by FERA into 21 high-technology items of manufacture. With this permission the large industrial houses falling within the purview of the MRTP Act and FERA companies were allowed to freely take up the manufacture of 83 items. Various other concessions like regularisation of excess

capacity and capacity re-endorsement, facilities to set up industries in backward areas etc. were also granted to MRTP and FERA companies.[3]

Delicensing. With a view to encouraging production, the government delicensed 28 broad categories of industries and 82 bulk drugs and their formulations. For these industries only registration with the Secretariat for Industrial Approvals was now required: no licence had to be obtained under the Industries (Development and Regulation) Act.

Re-endorsement of Capacity. With a view to improving capacity utilisation in industries, the government announced a scheme of capacity re-endorsement in April, 1982. During 1986, this scheme was liberalised to allow undertakings which had achieved 80 per cent capacity utilization (as against 94 per cent earlier) to avail of the facility. The re-endorsed capacity was to be calculated by taking the highest production achieved during any of the previous five years plus one-third thereof. The undertakings which were able to achieve capacity utilization equal to the re-endorsed level were to get further re-endorsement according to the highest production achieved in subsequent years. The number of industries for which automatic re-endorsement of capacity was not available was reduced from 77 to 26.

Broad Banding of Industries. The scheme of broad-banding of industries was introduced in 1984. This implied classification under broad categories—of two-wheelers, four-wheelers, tractors, as well as machinery for fertilisers, pharmaceuticals, and paper and pulp etc., into generic categories. Thus, to take one example, cars, jeeps, light, medium and heavy commercial vehicles, etc., were clubbed together into the generic category of "four wheelers". This measure was intended to enable the manufacturers to change their product-mix rapidly to match changes in demand patterns without incurring procedural delays and other costs associated with seeking amendments to their industrial licences. Broad-banding was extended in stages to cover 45 industry groups.

Minimum Economic Scales of Operation. Another important concept introduced in the field of industrial licensing was that of minimum economic level of operation. This was introduced in 1986. The idea was to encourage realization of economies of scale by expansion of existing installed capacities of undertakings to minimum economic levels of operation.

Development of Backward Areas. For promoting the development of backward areas, the government extended the scheme of delicensing in March 1986 to MRTP/FERA companies in respect of 20 industries for location in any centrally declared backward area and 23 non-Appendix I industries for location in category 'A' backward districts. The conditions permitting MRTP and FERA companies to establish non-Appendix I industries in backward districts were also liberalised.

Recognising that one of the impediments blocking the industrialisation of backward areas of the country is the absence of infrastructural facilities, the government announced the decision in 1988-89 to set up 100 growth centres spread across the country over a period of five years or so. It was decided to provide funds of the order of Rs. 25 crore to Rs. 30 crore to each growth centre for creating infrastructural facilities of a high order.

Incentives for Export Production. Various concessions were announced by government in its industrial policy and export-import policy from time to time to promote the expansion of exports. For example, MRTP and FERA companies were permitted (outside the Appendix I industries) if the product is predominantly for export. With a view to providing fillip to production in industries of high national priority and/or those meant exclusively for export, the government introduced Section 22-A in the MRTP Act whereby it could notify industries or services to which Sections 21 and 22 of the Act will not apply. In October 1982 all 100 per cent export-oriented industries set up in the Free Trade Zones were exempted from Sections 21 and 22 of the Act. In addition, the government identified some industries which were specially important from export angle. These industries were allowed 5 per cent automatic growth per annum, up to a limit of 25 per cent in a plan period over and above the normal permissible limit for 25 per cent excess production over the authorized capacity.

Enhancement of Investment Limit for SSI Units and Ancillary Units. As stated earlier, the July 1980 Statement fixed the investment limit for small-scale industries at Rs. 20 lakh and for ancillary units at Rs. 25 lakh. In March 1985 these limits were enhanced to Rs. 35 lakh and Rs. 45 lakh respectively. For tiny units, the investment limit stood at Rs. 2 lakh. A government notification issued in April 1991 raised the investment limit for small scale industry from Rs. 35 lakh to Rs. 60 lakh and for ancillary units from Rs. 40 lakh to Rs. 75 lakh. In August 1991, the investment limit for tiny units was raised to Rs. 5 lakh. In February 1997, the

investment limit for small-scale units and ancillary units was raised to Rs. 3 crore. The investment limit for tiny units was raised from Rs. 5 lakh to Rs. 25 lakh. The investment limit for small-scale industry was reduced to Rs. 1 crore in 1999 and remained at this level till 2006. With the passing of the SMED Act. 2006, the definition of small-scale enterprises has heen changed drastically with effect from October 2, 2006 (see Box 39.1 of chapter 39).

NEW INDUSTRIAL POLICY, 1991

In line with the liberalisation measures announced during the 1980s the government announced a New Industrial Policy on July 24, 1991. ***This new policy de-regulates the industrial economy in a substantial manner. The major objectives of the new policy are to build on the gains already made, correct the distortions or weaknesses that might have crept in, maintain a sustained growth in productivity and gainful employment, and attain international competitiveness.***[4] In pursuit of these objectives, the government announced a series of initiatives in respect of the policies relating to the following areas:

A. Industrial Licensing	B. Foreign Investment
C. Foreign Technology Agreements	D. Public Sector Policy
E. MRTP Act.	

A package for the Small and Tiny Sectors of industry was announced separately in August 1991 (discussed in detail in Chapter 39).

Abolition of Industrial Licensing

Industrial licensing policy in India has been governed by the Industries (Development & Regulation) Act, 1951. As we shall be discussing in detail in Chapter 32, industrial licensing policy and procedures have been liberalised considerably from time to time. Yet, the industrial licensing policy has all along been resented to by the entrepreneurs as it led to unnecessary governmental interference, delays in investment decisions and bureaucratic red-tapism, corruption etc. Not only this, the industrial licensing policy was also unable to achieve the objectives laid down for it by the government. On account of these considerations, and in order to liberalise the economy and to enable the entrepreneurs to make investment decisions on the basis of their own commercial judgement, the 1991 industrial policy abolished industrial licensing for all but 18 industries. The 18 industries for which licensing was kept necessary were as under—coal and lignite; petroleum (other than crude) and its distillation products; distillation and brewing of alcoholic drinks; sugar; animal fats and oils; cigars and cigarettes; asbestos and asbestos-based products; plywood and other wood based products; raw hides and skins and leather; tanned or dressed furskins; motor cars; paper and newsprint; electronic aeroscape and defence equipment; industrial explosives; hazardous chemicals; drugs and pharmaceuticals; entertainment electronics; and white goods (domestic refrigerators, washing machines, airconditioners, etc.). With the passage of time, most of these industries have also been delicensed. ***As of now, licensing is compulsory for only 5 industries. These are alcohol, cigarettes, hazardous chemicals, electronics aeroscape and defence equipment,and industrial explosives.***

In respect of delicensed industry, no approval is required from the government. However, entrepreneurs are required to submit an Industrial Entrepreneur Memorandum (IEM) to the Secretariat for Industrial Approvals (SIA) which acknowledges receipt. Since the announcement of new industrial policy till March 2007, 69,798 IEMs involving an estimated investment of Rs. 25,69,658 crore were filed. During the same period 4,241 LOIs (letters of intent) involving a proposed investment of Rs. 1,23,085 crore were filed.

Public Sector's Role Diluted

The 1956 Resolution had reserved 17 industries for the public sector. The 1991 industrial policy reduced this number to 8: (1) arms and ammunition, (2) atomic energy, (3) coal and lignite, (4) mineral oils, (5) mining of iron ore, manganese ore, chrome ore, gypsum, sulphur, gold and diamond, (6) mining of copper, lead, zinc, tin, molybdenum and wolfarm, (7) minerals specified in the schedule to the atomic energy (control of production and use order), 1953, and (8) rail transport. In 1993, items 5 and 6 were deleted from the reserved list. In 1998-99, items 3 and 4 were also taken out from the reserved list. On May 9, 2001, the government opened up arms and ammunition sector also to the private sector. ***This now leaves only 3 industries reserved exclusively for the public sector — atomic energy, minerals specified in the schedule to the atomic energy control of production and use order 1953, and rail transport.***

The new industrial policy also states that the government will undertake review of the existing public enterprises in low technology, small scale and non-strategic areas as also when there is low or nil social consideration or public purpose. Sick units will be referred to the Board for Industrial and Financial Reconstruction (or a similar body) for advice about rehabilitation and reconstruction. For enterprises remaining in the public sector, it is stated that they will be provided a much greater degree of management autonomy through the system of MOU (memorandum of understanding).

The government has also announced its intention to offer a part of government shareholding in the public sector enterprises to mutual funds, financial institutions, the general public and the workers. The disinvestment process was started in 1991-92 with the sale of minority stakes in some public sector undertakings. Since 1999-2000, the focus shifted to strategic sales. Over the period 1991-92 upto 2005-06, the government realised Rs. 49,214 crore from distinvestment. The new industrial policy indicates the government's intention to invite a greater degree of participation by the private sector in important areas of the economy.

MRTP Limit Goes

Under the MRTP Act, all firms with assets above a certain size (Rs. 100 crore since 1985) were classified as MRTP firms. Such firms were permitted to enter selected industries only and this also on a case-by-case approval basis. In addition to control through industrial licensing, separate approvals were required by such large firms for any investment proposals. The government felt that this was having a deleterious effect on many large firms in their plans for growth and diversification. The new industrial policy therefore scrapped the threshold limit of assets in respect of MRTP and dominant undertakings. These firms will now be at par with others, and not require prior approval from the government for investment in the delicensed industries. The MRTP Act has been accordingly amended. The now amended Act gives more emphasis to the prevention and control of monopolistic, restrictive and unfair trade practices so that consumers are adequately protected from such practices.

Freer Entry to Foreign Investment and Technology

As in the case of domestic industrial investment, foreign investment has also been traditionally regulated in India. In the case of both foreign technology agreements sought by Indian firms as well as foreign investment, it was necessary to obtain specific prior approval from the government for each project. It was argued that this caused undue delays and government interference and also hampered business decision-making. Therefore, the new industrial policy prepared a specified list of high technology and high-investment priority industries (listed in Annexure III) wherein automatic permission[5] was to be made available for direct foreign investment upto 51 per cent foreign equity. The industries in which automatic approval was granted included a wide range of industrial activities in the capital goods and metallurgical industries, entertainment electronics, food processing, and the services sectors having significant export potential. Besides, these included a number of other industries which are important for the rapid growth of the economy. The limit was subsequently raised from 51 per cent to 74 per cent and then to 100 per cent for many of these industries. ***Presently, foreign investment is permitted upto 100 per cent on the automatic route in most sectors subject to sectoral rules/regulations applicable. FDI is prohibited only in the following sectors : (1) retail trading (except single brand product retailing), (2) atomic energy, (3) lottery business, and (4) gambling and betting.*** For details regarding steps taken to promote foreign investment and technology in the period since 1991 please refer to the chapter on 'Foreign Investment, Technology and Multinational Corporations.'

Other Liberalisation Measures

Industrial location policy liberalised. In a departure from the earlier locational policy for industries, the new industrial policy stated that in locations other than cities of more than 1 million population, there will be no requirement of obtaining industrial approvals from the Centre, except for industries subject to compulsory licensing. In cities with a population of more than 1 million, industries other than those of a non-polluting nature, were required to be located outside 25 kms of the periphery.

Major amendments in the industrial location policy were effected during 1997-98. The requirement of obtaining industrial approvals from the Central government (except for the industries under compulsory licensing) for establishing units at locations not falling within 25 kms of the periphery of cities having a population of more than 1 million was dispensed with. However, notified industries of a non-polluting nature such as electronics, computer software and printing, may be located within 25 kms of the periphery of cities with more than 1 million population. Other industries are permitted only if they are located in designated industrial areas set up

prior to July 25, 1991. Zoning and Land Use Regulations as well as Environment Legislation continue to regulate industrial locations.

Abolition of Phased Manufacturing Programmes for new projects. To force the pace of indigenisation in manufacturing, Phased Manufacturing Programmes have been in force in a number of engineering and electronic industries. The new industrial policy has abolished such programmes in future as the government feels that due to substantial reforms made in the trade policy and the devaluation of the rupee, there is no longer any need for enforcing the local content requirements on a case-by-case, administrative basis. Various incentives that are currently available to manufacturing units with existing Phased Manufacturing Programmes will continue.

Removal of mandatory convertibility clause. A large part of industrial investment in India is financed by loans from banks and financial institutions. These institutions have followed a mandatory practice of including a convertibility clause in their loans into equity if felt necessary by their management. Although this option has not generally been exercised, it has often been interpreted as an unwarranted threat to private firms of takeover by financial institutions. The new industrial policy has provided that henceforth financial institutions will not impose this mandatory convertibility clause.

APPRAISAL OF NEW INDUSTRIAL POLICY

According to J.C. Sandesara, the new industrial policy seeks to raise efficiency and accelerate industrial production in five different ways:[6]

(1) A number of changes in industrial licensing policy, foreign investment, foreign technology agreements and MRTP Act are such as to do away with the prior clearance of the government. In such cases, project time and, therefore, project cost will be reduced. Material and human resources engaged in cultivating contacts and 'getting things done' will be released for more productive uses. Thus efficiency will improve.

(2) The changes in respect of foreign investment and foreign technology agreements are also designed to attract capital, technology and managerial expertise from abroad. This will raise the availability of such scarce resources in the country on the one hand, and will improve the level of efficiency of production on the other hand.

(3) Some changes as regards public sector may enhance the 'allocative efficiency'. Opening up of different areas (so far reserved for the public sector) to the private sector implies an opening for the sector which has, by and large, given a better account of itself. Closure, liquidation or rehabilitation etc. of sick/weak public sector units will free resources for more productive use. Similarly, privatisation may make for improved efficiency of the public sector, through its being subjected to the stock market discipline.

(4) Other measures in this area such as purposeful formulation and implementation of Memorandum of Understanding and its monitoring, professionalisation and greater autonomy may be expected to improve the performance of the enterprises that will remain in the public sector.

(5) Greater emphasis in controlling and regulating monopolistic, restrictive and unfair trade practices and the strengthening of powers of the MRTP Commission will curb anti-competitive behaviour of firms in the monopolistic, oligopolistic and ineffectively competitive markets and thus promote competition and efficiency.

However, the new industrial policy 1991 has invited scathing criticism from a number of quarters. The main points of criticism are as follows:

- Erratic and fluctuationg industrial growth
- Distortions in production structure
- Threat from foreign competition
- Dangers of business colonalisation
- Misplaced faith in foreign investment
- Personalistic relationships and practices continue to previal.

1. Erratic and fluctuating industrial growth. As noted above, the new industrial policy considerably reduced the interventionist barriers to the entry of domestic and foreign investors, resulting in what has been proclaimed as a much more competitive environment in the industrial sector. It was hoped that this 'much more competitive environment' would, in itself, induce higher growth rates in the industrial sector. However, this has not happened. In fact, the rate of growth in the industrial sector declined in the post-reform decade (particularly during the latter half of 1990s). For instance, the rate of growth of industrial production was only 5.0 per cent per annum during the period of the Ninth Plan (1997-78 to 2001-02) whereas it was 7.8 per cent per annum

in the pre-reform period (1980-81 to 1991-92). During 1990s as a whole (1990-91 to 1999-2006) the rate of growth of industry was only 5.7 per cent per annum. What is more, the industrial sector has witnessed erratic and fluctuating growth rates in different years leading to conditions of instability and uncertainty. However, the industrial sector registered strong positive growth of 8.0 per cent per annum during the period of the Tenth Plan (2002-03 to 2006-07).

2. Distortions in production structure. From the point of view of long run industrial development, the most important group of industries is the group of capital goods industries. However, the rate of growth of this group of industries fell drastically from 9.4 per cent per annum in the pre-reform decade to only 4.7 per cent over the Ninth Plan period. This points to the distortions in the production structure during 1990s. However, the capital goods sector registered robust growth of 14.4 per cent per annum during the Tenth Plan period (2002-03 to 2006-07).

3. Threat from foreign competition. In the early euphoria of liberalisation, the private sector industrialists welcomed the new industrial policy 1991 but they soon came to realise that opening up the Indian economy to foreign competition meant more and cheaper imports, more foreign investment, opportunities to the MNCs (multinational corporations) to raid and takeover their enterprises, and worse, their inability to meet the challenge from MNCs due to their weak economic strength *vis-a-vis* the MNCs. In the new liberalised scenario that has emerged in the post-1991 reform phase, the Indian businessmen are facing unequal competition from MNCs. The 'unequal competition' stems from a number of reasons discussed in detail in the sub-section on 'Effects of Globalisation' of the chapter on 'Globalisation and its Impact on Indian Economy'. As stated therein, the Indian enterprises suffer from 'size disadvantages' as they are just minuscules in comparison with MNCs; they have for long operated in a protectionist environment which promoted inefficiencies in production; the cost of capital to Indian business is much higher than for MNCs; they are very weak financially in comparison with MNCs; high, multiple and cascading indirect taxes—especially at the local level, where they are not applicable to foreign imports—result in making Indian goods uncompetitive; etc. On account of these reasons, the Indian industry associations (particularly the Confederation of Indian Industry) have recently adopted a very critical attitude to the government's new industrial policy. The basic position of CII is that India has moved from too much protection to too little protection, which may eventually result in policy-induced de-industrialisation.[8] The overall business demand is for a *level playing field.*

4. Dangers of business colonalisation. The various measures to promote foreign investment contained in the new industrial policy and the various concessions to such investment announced in recent years have provided opportunities to MNCs to penetrate the Indian economy and gobble up Indian enterprises. Baldev Raj Nayar has pointed out three strategies adopted by the MNCs to penetrate the Indian economy through FDI (foreign direct investment).[9] One, some foreign investors have bought off existing local brands alongwith their branded products with the aim of replacing such products with their own internationally known products, eliminating in the process the possibility of competition from the local products. Two, some foreign investors initially opted for joint ventures with Indian partners to gain easy foothold in the domestic industry but, once having consolidated their position, reduced the Indian partner to a subordinate position or simply ousted him. Thus many Indian businessmen feel that MNCs simply use them as a 'door mat' for entry and spread risk only to be dumped later. Three, some foreign investors, even as they started out with local partners in a joint venture, then went on to set up parallel 100 per cent subsidiaries of their own in the same field, which were then favoured with greater sources and more modern technology, rendering the joint venture uncompetitive and useless. The aggression which MNCs have shown to devour domestic enterprise has raised the dangers of business colonalisation.

5. Misplaced faith in foreign investment. Various policy pronouncements of the government in recent years indicate that it expects foreign investment to help in technological upgradation of the industrial sector and push up export earnings. However, this faith in foreign investment is misplaced. As pointed out by H.K. Paranjape, none of the MNCs operating in this country has attempted to develop India as an important base for a significant part of its world-wide research and development work. Despite various tax concessions and incentives none of the multinationals tried to expand export markets. They undertook export activities only to the extent they were compelled to do so under export obligations, or when it was found necessary to do so in order to earn foreign exchange for importing some of their essential requirements. In fact, instead of developing India as a major production and export base, many MNCs have only attempted to use their international trade capacities and contacts mainly for exporting goods manufactured by other —usually small scale—units. Thus they have operated more as trading than as manufacturing and exporting concerns.[10]

Coming to the import of foreign technology, Paranjape again expresses some reservations. According to him, in the whole eagerness to import foreign technology, little attention seems to have been paid to the possibility that production and managerial technologies found more suitable in other countries may not necessarily prove to be the best in our circumstances. As correctly pointed out by him, one of the very purposes of India's industrialisation is to ensure that our very large manpower resources are effectively utilised. This implies the adoption of labour-intensive and capital saving technologies in whichever areas it is feasible to do so. This may imply major readjustments in technologies that have developed in the labour scarce and capital abundant rich countries. This will not be an easy task. Moreover, despite talks of globalisation, many rich countries are reluctant to permit unrestricted export of technologies as, in many areas, technologies are common for civilian and defence - related items. MNCs which make a technological breakthrough are also usually reluctant to permit the use of their up-to-date technologies even by their subsidiaries unless these are located in politically 'safe' countries. India obviously does not satisfy this criterion from the view point of these MNCs, or the defence authorities of the USA and other rich countries.

6. Personalistic relationships and practices continue to prevail. The 'licence permit raj' of the pre-1991 period provided ample scope for rent seeking as the entire operations of the industrial licensing policy were governed by personalistic relationships. According to John Degnbol-Martinussen while de-licensing and de-regulation has undoubtedly discouraged rent seeking and corruption at the Central government level, these practices have continued and may have even increased at the State government level. This is due to the reason that while the number of interaction points between government officials and entrepreneurs have declined at the Union level, they have generally increased at the State level providing ample scope for continued interaction on a personalistic basis.[11]

NOTES

1. Industries (Development and Regulation) Act, 1951 is discussed in detail in Chapter 32.
2. Jagdish Bhagwati and Padma Desai, *India: Planning for Industrialisation* (London: Oxford University Press, 1970), p. 143.
3. For a detailed discussion refer to the chapter on "MRTP Act, 1969 and Competition Act, 2002" and the chapter on "Foreign Investment, Technology and Multinational Corporations."
4. Government of India, *Handbook of Industrial Statistics*, 2001, p.10.
5. Under the automatic route, prior approval is not required; only the reporting stipulations have to be met for monitoring purposes. Thus automatic approval reduces the scope of discretionary use of powers by the Foreign Investment Promotion Board.
6. J.C. Sandesara, "New Industrial Policy: Questions of Efficient Growth and Social Objectives", *Economic and Political Weekly,* August 3-10, 1991, p. 1970.
8. John Degnbol Martinussen, *Policies, Institutions and Industrial Development* (New Delhi, 2001), p. 151.
9. Baldev Raj Nayar, *Globalization and Nationalism* (New Delhi, 2001), pp. 173-4.
10. H.K. Paranjape, "New Industrial Policy: A Capitalist Manifesto," *Economic and Political Weekly,* October 26, 1991, p. 2476.
11. John Degnbol-Martinussen, *op. cit.,* pp.205-06.

CHAPTER

28 EXPORT IMPORT POLICY AND TRADE LIBERALISATION

Import Policy: The Pre-Reform Period
• Import Restrictions • Import Substitution • Import Liberalisation in 1980s • A Critical Evaluation of Import Policy
Export Policy: The Pre-Reform Period
• The Three Phases of Export Policy • Export Promotion Policies: An Overall View • Organisational Structure for Promotion of Exports • A Critical Evaluation of Export Policy
New Trade Policy: The Reform Period
• Features of New Trade Policy • A Critical Evaluation of the New Trade Policy
Foreign Trade Policy (2004-09)
• Main Features of FTP, 2004-09 • A Critical Evaluation of FTP • Third Supplement to FTP announced in April 2007

During recent years, because of the increasing focus on trade liberalisation and globalisation, foreign trade policy has assumed great significance. In this chapter, we propose to undertake a detailed discussion on Government of India's trade policy. This discussion is best divided into two periods: (1) the pre-reform period (*i.e.* the period prior to 1991), and (2) the reform period (*i.e.* the period after 1991). This is due to the reason that ***the year 1991 is a 'watershed' in trade policy as massive trade liberalisation measures adopted since this year mark a major departure from the relatively protectionistic trade policies pursued in earlier years.***

We shall address the following questions in this chapter :

- What were the main features of India's import and export policies in the pre-reform period ?
- What were the shortcomings of these policies?
- What measures were taken by the Government of India in the post-reform period to liberalise foreign trade ?
- What are the objectives and strategies of foreign trade policy, 2004-09 ? What are the main features of this policy ? What are the shortcomings of this policy ?

IMPORT POLICY: THE PRE-REFORM PERIOD

The import policy of the Government of India in the pre-reform period had two important constituents: (*i*) import restrictions and (*ii*) import substitution. It was formulated keeping in view the limited foreign exchange reserves of the country, shortages of essential consumer goods in the economy, requirements of capital goods, machinery, spare-parts and components for the building up of heavy, basic industries, and the role and scope of import substitution in the country. The period of 1980s was characterised by massive import liberalisation — the desire being to enhance the export competitiveness of large sections of Indian industry. Thus, the discussion on import policy in the pre-reform period incorporates a discussion on

- Import restrictions
- Import substitution
- Import liberalisation in 1980s.

Import Restrictions

The Mahalanobis strategy of development encouraging large-scale industrialization of the country was initiated in the Second Five Year Plan (which started in 1956-57). Under this strategy of development the government had to import capital equipment, machinery, components, spare-parts, industrial raw materials, intermediate goods, technical know-how etc. in large quantities and this led to a substantial increase in foreign exchange expenditure. The government also had to resort to import of foodgrains from time to time to overcome the shortage of foodgrains. As against this, the export earnings continued to be stagnant. Thus the government had no option but to severely curtail import expenditure. Therefore ***the history of severe import restrictions in the country starts from the year 1956-57.*** Given the acute shortage of foreign exchange most of the time, policymakers opted for direct allocation of foreign exchange among different users and uses through import licences. "An import licence allowed a *specified amount* of a *specified item* to be imported by a *specified user* for a *specified purpose* sometimes even from a *specified* source of supply."[1] As noted by Tendulkar and Bhavani, Quantitative Restrictions (QRs) were selective in the sense that the specified ceiling limits were different for the imports of different items depending on the perceived importance in the development strategy. For instance, limits were high and liberal in the case of capital goods imports, and zero, low, and'rigid for the imports of 'non-essential' consumer goods. The operation of this cumbersome policy required comprehensive details and a complex administrative mechanism. For the purpose, imports were divided into different categories, namely consumer goods, intermediate goods and capital goods. Each category was sub-divided into *non-permissible* (banned), *limited permissible* (with mandatory certification and mandatory clearance from the Chief Controller of Imports and Exports CCI&E), *automatic permissible* (with mandatory certificate but with clearance from the CCI&E), and *open general licence* (OGL, without certification and without clearance of the CCI&E) groups. Licences were categorised further based on user type such as established importer, actual user, newcomer, *ad hoc,* export promotion scheme (like import replenishment licence), and others (like replacement licence). Some of the imports were allowed only through state trading agencies like State Trading Corporation (STC), Minerals and Metals Trading Corporation (MMTC) etc. (these were known as canalised items). As the foreign exchange difficulties continued to mount up, more and more items were brought under import restrictions. ***The policy of import restrictions was rigorously pursued by the government for full two decades right upto 1977-78.*** However, there was a brief period of import liberalisation after the devaluation of 1966.

Import Substitution

The two broad objectives of the programme of import substitution in India were: (a) to save scarce foreign exchange for the import of more important goods, and (b) to achieve self-reliance in the production of as many goods as possible. These objectives were achieved by the selective use of QRs as this regime was used to provide automatic and custom-made protection to any activity that substituted imports.[2] The import substitution policy in India has gone through various phases. Broadly speaking, we can discern three distinct phases: (*i*) in the earlier phase, import substitution mostly took the form of domestic production of consumer goods; (*ii*) in the second phase, emphasis shifted to the replacement of the import of capital goods; and (*iii*) in the third phase emphasis was on reducing the dependence on imported technology by developing and encouraging the use of indigenous techniques. As a result of the policy of import substitution, the structure of imports has undergone significant changes. Many items which were previously imported are now being produced in the country itself. As a result of this policy, the country has been able to increase the production of many industrial products like iron and steel, automobiles, railway wagons, machine tools, diesel engines, power transformers etc., and in the case of many other products has achieved a stage of self-sufficiency.

Import Liberalisation in 1980s

The import policy of the Government of India till 1977-78 varied in degrees of restrictiveness during different plans. It was rather light during the First Plan, intensely severe during the Second, somewhat less so during the Third (except in the last two years); and perhaps equally so since then (right up to 1977-78). ***The year 1977-78 initiated a new era of import liberalisation in the country. This process was carried forward in 1980s.*** The annual import policies of 1980-81 to 1984-85 followed the liberal approach of providing necessary imported inputs for the industrial sector. However, the real thrust in the direction of liberalisation was provided from 1985 onwards when the system of formulating long term (three year) policies was adopted.

Three long-term export-import policies were announced by the government. The first covered the period 1985 to 1988, the second covered the period 1988 to 1990 and the third covered the period 1990-92. The broad details of import liberalisation measures enunciated in these export-import policies are outlined below:

1. Policy for Import of Capital Goods. Since capital equipment is the basic requirement of the industrial sector, the approach in the three-year export-import policies was on providing easy access to imported capital items by progressively delinking them from licensing formalities. A large number of capital goods were placed under OGL (Open General Licence) category *i.e.* they could be imported without any import licence.

2. Policy for Import of Raw Materials. As in the case of capital goods, a large number of raw materials, components and consumables were placed under OGL in order to enable the actual users (industrial) to procure them without going through the licensing formalities. In addition to OGL imports, actual users (industrial) were extended the facility of importing raw materials, components and consumables under supplementary licences.

3. Import Policy for Registered Exporters. Because of the dire need for increasing the export earnings of the country, import policies in 1980s were given an 'export orientation'. The aim of these policies was to provide the Registered Exporters an assured, continuous and uninterrupted supply of the required production inputs, essential for expanding the exports on a sustaining basis. Duty free import of raw materials against REP (Registered Exporters Policy) licences was introduced. Registered exporters were provided with the facility to import capital goods against REP licences.

4. Policy for Export/Trading Houses. Exporters who fulfil certain minimum export requirements for a specified period of time were granted the status of Export Houses, Trading Houses, Star Trading Houses or Super Star Trading Houses. The 1988-90 policy had fixed the eligibility limit for recognition as Export Houses and Trading Houses at Rs. 2 crore and Rs. 10 crore of net foreign exchange earning respectively. This was raised to Rs. 5 crore for Export Houses and Rs. 20 crore for Trading Houses by the 1990-92 policy. The latter policy also introduced a new category of Star Trading Houses. These included those Trading Houses that had net foreign exchange export earning at Rs. 75 crore or above annually in the preceding three years. In view of their special position in the field of exports, Export/Trading Houses were provided with a number of import benefits.

5. Policy for Import of Technology. The government allowed liberal import of technology with a view to making export production of the country internationally competitive and also to help in the country's technological advancement. However, the emphasis was on the absorption and adaptation of imported technology.

A Critical Evaluation of Import Policy

In this sub-section we present a critical evaluation of the import control regime, the policy of import substitution and the policy of import liberalisation of the pre-reform period.

1. The Import Control Regime. According to Jagdish Bhagwati and Padma Desai,[3] ***import policy had the following adverse economic effects: (1) delays; (2) administrative and other expenses; (3) inflexibility; (4) lack of co-ordination among different agencies; (5) absence of competition; (6) bias towards creation of capacity despite underutilisation; (7) anticipatory and automatic protection afforded to industries regardless of costs; (8) discrimination against exports; and (9) loss of revenue.***

In addition to the above, the import control regime resulted in widespread corruption. According to T.N. Srinivasan, "Given that QRs on imports were substantially below market demand, the domestic price of an imported commodity far exceeded its land cost inclusive of tariff duties and other taxes. As such there were rents associated with a licence to import. Thus ***the power to grant a licence meant power to confer the right to the rent involved.*** Since the domestic price of an imported commodity, and hence the rent to be earned per unit of import, would depend on the total quantity of imports allowed in, the licensing authority not only conferred the right to the rent but also determined its amount."[4] Thus the entire system of import licence allocation bred corruption.

2. The Policy of Import Substitution. The policy of import substitution enabled the country to achieve diversification and depth so necessary for further growth. However, many economists have argued that the indiscriminate extension of import substitution to a wide range of sectors in India without regard to costs, was not the 'best', or the 'most efficient' policy. In this context Jaleel Ahmed states, "Valuable resources could have been saved if the process of import substitution had been more selective with a limited number of strategically chosen sectors and industries, where a concentration of effort and resources could have maximised the gains in efficiency. In the heavy industry sector, in particular, simultaneous development of a plethora of manufacturing activities may have deprived the economy of the advantages of large-scale production and of meeting the minimum critical thresholds."[5] Another important criticism is that since under the policy of import substitution, the import of most luxury consumer goods was restricted by prohibitory tariffs, the profitability of their domestic production automatically increased. This factor, coupled with the political pressure of the affluent to

satisfy their demand, led to the establishment of a wide range of import-substituting consumer goods industries catering to the demand of the affluent few for sophisticated and highly diversified products, totally out of line with the average per capita income in the country. The demand tended to fall off after a certain point (because of the general poverty of the masses) resulting in unutilized capacity and higher average costs in these luxury goods industries.

3. The Policy of Import Liberalisation. The policy of import liberalisation pursued with a vigour in the 1980s resulted in a substantial increase in the volume of imports. For instance, the volume index of imports was 224.2 in 1988-89 (base 1978-79 = 100), *i.e.*, in a period of a decade, it had more than doubled. Also, import liberalisation led to a significant increase in the import intensity of exports. In his study covering the period 1970-85, Deepak Nayyar has shown that the import-intensity of exports increased from 6.9 per cent in 1972-73 to 23.5 per cent as a proportion of total exports in 1984-85 and from 10.4 per cent to 38.5 per cent as a proportion of exports eligible for REP facilities (excluding gems and jewellery for which the import content was very high).[6] Some data for the later period are available in Reserve Bank's study on Finances of Public Limited Companies which covers 1942 public limited companies. This study shows that the import intensity increased by almost 25 per cent over a three year period (1984-85 to 1986-87) which is quite substantial.

While the impact of the policy of import liberalisation in increasing the import-intensity is thus fairly well established, its impact on promoting exports is a bit difficult to judge particularly because there are a number of factors affecting the export performance and import liberalisation is just one of them. However, Deepak Nayyar notes that while the volume of exports had increased by 58 per cent and unit value of exports by 122 per cent during 1970-71 to 1977-78, export growth during 1977-78 to 1984-85 was marked by a sharp deceleration as the volume of exports grew by only about 30 per cent and the unit value of exports by 68 per cent.[7] Thus during the earlier period of liberalisation, import liberalisation did little for export promotion. On the other hand, as the import content of exports increased, the proportion of net-foreign exchange earnings in gross *f.o.b.* value of exports actually declined.

EXPORT POLICY: THE PRE-REFORM PERIOD

The Three Phases of Export Policy

Bimal Jalan classifies the export policy of the Government of India in the pre-reform period into three distinct phases: Phase I (upto the first oil shock of 1973), Phase II (covering the period from 1973 upto a decade or so), and phase III (the period after the above and covering roughly the latter half of the Sixth Plant and the whole of the Seventh Plan). The period of Phase I can be divided into two sub-periods: (*a*) 1952-66, and (*b*) 1966-73. ***The first sub-period covers the first three Five Year Plans and was characterised by an essentially passive export policy*** though some steps to increase exports were undertaken in the Third Plan. Except for a few items such as iron ore, stagnation of export earnings in this period is to be largely attributed to domestic policies which often led to the falling share of India's traditional exports and insufficient expansion in the case of non-traditional exports. The second sub-period in Phase I starts with the devaluation of rupee by 36.5 per cent in terms of gold in June 1965. The government expressed the hope that the devaluation would lead to expansion in export earnings as Indian goods would now be cheaper in international markets. On the other hand, imports will decline as the prices of imported goods would increase.

Phase II can be considered to have begun in 1973 and lasted for about a decade. "In this phase, although this was not explicitly stated, it was recognized that import substitution policies by themselves could not bring about a viability in India's balance of payments... In this second phase exports were, therefore, accorded a high priority."[8] ***The government, accordingly, undertook a number of steps to increase exports.*** Moreover, as pointed out by Deepak Nayyar, the nominal effective exchange rate (NEER) of the rupee depreciated continuously in the 1970s. Given the lower rate of inflation at home as compared to the outside world, this also meant a sharp downward movement in the real effective exchange rate (REER) of the rupee. As a result, the relative profitability of exports increased.

Phase III saw a more positive approach to export promotion strategy. While incentives for export production were enhanced on the one hand, exports themselves were now being seen as an integral part of industrial and development policies. Export policy in Phase III emphasized technological upgradation, increase in the size of plants, freer imports and domestic and international competition for the entire industrial sector as being essential for export promotion.

Export Promotion Policies: An Overall View

Important export promotion measures undertaken by the Government of India during the pre-reform period were as follows:

1. Cash Compensatory Support (C.C.S.). This was introduced in 1966. It was designed to provide compensation for unrebated indirect taxes paid by exporters on inputs, higher freight rates, and market development costs. The rates varied from product to product, and often from exporter to exporter. The scope of CCS was steadily extended over the years and the proportion of total exports eligible for CCS rose from a level of about 20 per cent in the early 1970s to a little more than 40 per cent in the early 1980s. The CCs involved the largest single budgetary outlay for exports.

2. Duty Drawback System. The objective of the duty drawback system is to reimburse exporters for tariff paid on the imported materials and intermediates and central excise duties paid on domestically produced inputs which enter into export production. This is a world-wide practice and the rationale is straight forward. Custom duties and excise duties on inputs raise the cost of production in export industries and thereby affect the competitiveness of exports. Therefore, exporters need to be compensated for the escalation in their costs attributable to such customs and excise duties.

3. Replenishment Licences. In order to provide the export sector of the economy with access to importable inputs that enter into export production, at international prices, the import policy allowed special import facilities for registered exporters. In 1957, the government introduced the Import Entitlement Scheme (IES) to help the exporters in procuring imported raw materials and other components necessary for export production. Exporters were granted import licences, fetching high import premia, pro rata to the value of exports effected. IES was withdrawn on devaluation of the Indian rupee in 1966 but was soon reintroduced in another garb in a revised form. The new name of the scheme was Import Replenishment Scheme (IRS). The system of import replenishment licences which were related to the *f.o.b.* value of exports was, for most part, a facility in so far as it enabled exporters to import inputs where the domestic substitutes were not adequate in terms of price, quantity or delivery dates; it was also an incentive in so far as there was a premium on those REP licences which were transferable.

4. Advance Licences and Duty Exemption Scheme. Advance licences facilitated imports of specified raw materials without payment of any customs duty. Such licences were available only against confirmed export orders and/or letters of credit.

5. EPZs and 100 per cent EOUs. With a view to giving impetus to export drive, the government set up Export Processing Zones (EPZs) which provide almost free trade environment for export production so as to make Indian export products competitive in the world market. The scheme of 100 per cent Export Oriented Units (EOUs) was introduced in December 1980 to provide duty free access to imports of raw materials, intermediate goods, capital goods and technology on OGL. Their production is bonded for exports and the units can be established anywhere in the country.

6. Fiscal Concessions for Exports. Special fiscal treatment granted to exports took two forms, that which related to the payment of indirect taxes, and that which related to the payment of direct taxes. The first type of concession was incorporated in the duty drawback system and the regime of cash compensatory support which sought to reimburse indirect fares that were not refunded through the former. The second type of concession was incorporated in income tax provisions where earnings from exports were either partially exempted from income tax, or taxed at a lower rate.

7. Export Credit and Assistance to EPCs. Assistance was granted in the form of grants-in-aid to the Export Promotion Councils and approved organisations, export houses, consultancy organisations and individual exporters to undertake (*a*) market research, commodity research, are a survey etc, (*b*) export publicity and dissemination of information, (*c*) trade delegations and teams, (*d*) participation in trade fairs and exhibitions, (*e*) estalishment of offices and branches in countries abroad, (*f*) research and development schemes etc., and (*g*) any other scheme that would promote the development of market for Indian goods abroad.

A Critical Evaluation of Export Policy

1. Absence of a long term export strategy. As noted earlier, phase I (*i.e.* the period from the beginning of the planning to the first oil shock of 1973) was characterised by export pessimism. In the first two plans, estimates were more in the nature of expected earnings rather than of firm targets and no definite programme of expanding export earnings was adopted. Indeed, the Second Plant took the position that only when

industrialisation had proceeded some way that increased production of home would get reflected in large-export earnings. Some measures of export subsidization were indeed started in the Third Plan yet the overall mood of pessimism persisted. Although in phases II and III, more attention was paid to the export sector yet the task of 'integrating' export planning with the overall planning could not to be accomplished.

2. Problems confronting primary exports. For a long period of time, primary products contributed a major portion of India's export earnings. However, prospects of increasing exports of these commodities were limited on account of a number of external and internal factors. The external factors included (*i*) steady deterioration in the terms of trade for primary products in the international market; (*ii*) severe fluctuations in international product prices; (*iii*) growth of synthetic substitutes; (*iv*) changes in technology which have reduced the amount of material used in manufacturing; (*v*) pattern of consumption in developed countries which makes for a low propensity to consume such products; and (*vi*) tariff and other restrictions imposed by industrial countries on some primary products. International demand for most of the primary products exported by India had remained stagnant while it had to face serious competition from some other underdeveloped countries interested in increasing their exports of these goods. As result, earnings from exports of primary products failed to increase much.

3. Irrational export policy measures. The rationale for most of the export assistance schemes was that Indian exporters should be compensated for the excess costs they incurred compared with their competitors because of other distortions in the Indian economy. However, as noted by T.N. Srinivasan, "since these excess costs were hard to quantity, there was no way to establish that the total assistance received under various incentive schemes to which a potential exporter was entilted was more or less than necessary to induce him to export."[9] Moreover, the bureaucratic requirement to be met to claim the assistance under the export incentive schemes was unnecessarily complex, time consuming and costly.

4. Trading problems. These include external impediments which posed a problem of "entry" for the Indian manufactures (and manufactures of other developing countries) in markets of industrialised countries. The most important factor inhibiting exports of manufactured products from less developed countries to developed countries is the system of tariffs adopted by the latter. The characteristic feature of this system is that tariff rates become increasingly higher as one moves from raw material to manufactured product. For example, as one moves from iron ore to raw steel and then to machine goods, the tariff rates in industrialized countries frequently increase. Such a tariff system makes it difficult for less developed countries to compete in the world market for manufactures. This discriminatory tariff system is accompanied by a plethora of quota restrictions and other non-tariff barriers. Another external impediment is that the process of import substitution in other countries encompasses virtually the same range of goods which India is trying to export. The most glaring example in this context is of the cotton textile industry which many less developed countries have developed successfully in the post war period.

5. Production problems. A serious problem as far as exports of Indian manufactured products is concerned is the lack of 'technological dynamism' in Indian industry. In spite of changes in the industrial and trade policies, most Indian firms continue to produce outdated products with inefficient production technologies. Not only this, a very large number of firms continue to use plants which are more than 20 years old. These plants suffer from frequent breakdowns, poor and uneven product quality, and high rejection rates. They have also become inefficient users of energy. Furthermore, these plants embody obsolete production technologies which have been replaced by more advanced and efficient technologies in the developed countries.

NEW TRADE POLICY: THE REFORM PERIOD

As stated earlier, the period after 1991 has been marked by a substantial liberalisation of the trade policy. While some liberalisation measures were the result of the conviction among government circles that they were necessary to make exports competitive in the international market, some were undertaken under the pressure of the international agencies, as a part of the stabilisation and structural adjustment programme. Moreover, with India joining the WTO (World Trade Organisation) in 1995 as a founder member, it is under an obligation to strike down all quantitative restrictions on imports and reduce import tariffs so as to 'open up' the economy to world trade and the forces of globalisation.

Features of New Trade Policy

The main features of the new trade policy as it has evolved over the years since 1991 are as follows:

1. Freer Imports and Exports. In the pre-reform period, India's trade policy regime was complex and cumbersome. There were different categories of importers, different types of import licences, alternate ways of importing etc. Substantial simplification and liberalisation in all these respects has been carried out in the reform period. The tariff-line wise import policy was first announced on March 31, 1996 and at that time itself 6,161 tariff lines were made free. Till March 2000, this total had gone up to 8,066. Quantitative restrictions in respect of 1,429 tariff lines remained till this date. The Exim Policy 2000-01 removed quantitative restrictions on 714 items and the Exim Policy 2001-02 removed quantitative restrictions on the balance 715 items. Thus, ***in line with India's commitment to the WTO, quantitative restrictions on all import items have been withdrawn.***

2. Rationalisation of Tariff Structure. In its Final Report published in January 1993, Chelliah Committee had advocated drastic reductions in import duties. The Committee expressed the opinion that the rupee had depreciated considerably in the 1980s and the early 1990s, pushing up the level of protection to Indian industries considerably. For instance, the Committee pointed out that in the seven year period 1985-86 to 1992-93, the real exchange rate of the rupee had depreciated by 57.45 per cent. This had pushed up the cost of the imports considerably leading to very high levels of protection to the Indian industry. The Committee, therefore, recommended that the prevailing import duties be rationalised and drastically lowered by 1998-99 so that parity in prices of goods produced domestically and internationally can be established. Acting on the recommendations of the Committee, the Government has, over the years, reduced the maximum rate of duty. The 1993-94 Budget had reduced it from 110 per cent to 85 per cent. The successive Budgets have reduced it further in stages. ***The peak import duty on non-agricultural goods is now only 10 per cent.***

3. Decanalisation. A large number of exports and imports used to be canalised through the public sector agencies in India. The supplementary trade policy announced on August 13, 1991 reviewed these canalised items and decanalised 16 export items and 20 import items. The 1992-97 policy decanalised imports of a number of items including newsprint, non-ferrous metals, natural rubber, intermediates and raw materials for fertilisers.

4. Convertibility of Rupee on Current Account. The government made a two-step downward adjustment of 18-19 per cent in the exchange rate of the rupee on July 1 and July 3, 1991. This was followed by the introduction of partial convertibility of rupee in 1992-93. Under this system a dual exchange rate was fixed under which 40 per cent of foreign exchange was to be surrendered at the official exchange rate while the remaining 60 per cent of foreign exchange was to be converted at a market determined rate. The 1993-94 Budget introduced full convertibility on trade account. As a result, the dual exchange rate system was dispensed with and a unified exchange rate system introduced. Under the unified exchange rate system regime, the 60:40 ratio was extended to 100 per cent coversion for (*i*) almost the entire merchandise trade transactions (*i.e.* export and import of goods); and (*ii*) all receipts, whether on current or capital account of balance of payments (BoP), but not all payments. ***India achieved full current account convertibility in August 1994*** when the Reserve Bank further liberalised payments and accepted obligations under Article VIII of the IMF, under which India in committed to foresake the use of exchange restrictions on current international transactions as an instrument in managing the balance of payments.

The experience with the market determined exchange rate system has been satisfactory. For most of the period since 1993, the foreign exchange market has been characterised by orderly conditions, excepting a few episodes of volatility. The exchange rate of the rupee was $ 1 = Rs. 39.30 on January 18, 2008.

5. Trading Houses. The 1991 policy allowed export houses and trading houses to import a wide range of items. The Government also permitted the setting up of trading houses with 51 per cent foreign equity for the purposes of promoting exports. Under the 1992-97 trade policy, export houses and trading houses were provided the benefit of self certification under the advance licence system, which permits duty free imports for exports.

The 1994-95 policy introduced a new category of trading houses called Super Star Trading Houses. To attain the status of a Super Star Trading house, an exporter must have registered an average FOB value of exports of Rs. 925 crore during the preceding three years or Rs. 1,387.50 crore during the preceding year. On the basis of NFE criterion, an exporter must have registered an average net foreign exchange (NFE) value of exports of Rs. 740 crore during the preceding three years or Rs. 1,100 crore during the preceding year. These houses were to be entitled to membership of apex consultative bodies concerned with trade policy and promotion, representation in important business delegations, special permission for overseas trading, and special import licences at enhanced rate.

6. Special Economic Zones. A scheme for setting up Special Economic Zones (SEZs) in the country to

promote exports was announced by the government in the Export and Import Policy on March 31, 2000. During 2005-06, exports from functioning SEZs were around $ 5 billion. To instil confidence in investors and signal the government's commitment to a stable SEZ policy regime, the Special Economic Zones Act, 2005, was passed by Parliament in May 2005. The SEZ Act, 2005, supported by SEZ Rules, came into effect on February 10, 2006. The main objectives of the SEZ Act are generation of additional economic activity, promotion of exports of goods and services, promotion of investment from domestic and foreign sources, creation of employment opportunities and development of infrastructure facilities. Various incentives and facilities are offered to both units in SEZs for attracting investments into SEZs (including foreign investment) as well as for SEZ developers. It is expected that these incentives and facilities will trigger a large flow of foreign and domestic investment in SEZs, in infrastructure and productive capacity, leading to generation of additional economic activity and creation of employment opportunities. For details on the SEZ Policy, please see Box 28.1.

BOX 28.1. Policy on Special Economic Zones (SEZs)

- India was one of the first in Asia to recognise the effectiveness of the Export Processing Zone (EPZ) model in promoting exports, with Asia's first EPZ set up in Kandla in 1965. Seven more zones were set up thereafter. However, the zones were not able to emerge as effective instruments for export promotion on account of the multiplicity of controls and clearances, the absence of world class infrastructure and an unstable fiscal regime.

SEZ Policy, 2000

With a view to overcome the above shortcomings and attract larger foreign investments in India, the Special Economic Zone (SEZ) Policy was announced in April 2000. The main difference between an SEZ and EPZ is that the former is an integrated township with fully developed infrastructure whereas an EPZ is just an industrial enclave. The SEZ Policy, 2000, was intended to make SEZs an engine for economic growth 'supported by quality infrastructure complemented by an attractive fiscal package, both at the Centre and the State level, with minimum possible regulations. Under the new scheme all existing zones were converted into SEZs. However, the impact of SEZs remained far removed from expectations.

SEZ Act, 2005

In order to provide a significant thrust to the policy, the government enacted the SEZ Act, 2005. The Act became operative in February 2006 after the SEZ rules were framed and notified. The salient features of the Act are as follows:

- **Governance.** An important feature of the Act is that it provides a comprehensive SEZ policy framework to satisfy the requirements of all principal stakeholders in an SEZ. Another major feature of the Act is that it claims to provide expeditious and single window clearance mechanisms. The responsibility for promoting and ensuring orderly development of SEZs is assigned to the Board of Approval (BOA) to be constituted by the Central Government.
- **Incentives.** The Act offers a highly attractive fiscal incentive package, which ensures *(i)* exemption from custom duties, central excise duties, service tax, central sales tax and securities transactions tax to both the developers and the units; *(ii)* tax holidays for 15 years, i.e., 100 per cent tax exemption for 5 years, 50 per cent for the next 5 years, and 50 per cent of the ploughed back export profits for the next five years; and *(iii)* 100 per cent income tax exemption for 10 years in a block period of 15 years for SEZ developers.
- **Infrastructure.** Provisions have been made for *(i)* the establishment of free warehousing zones to create world class trade-related infrastructure to facilitate export of goods aimed at making India a global trading-hub; *(ii)* the setting up of offshore banking units and units in an international financial service centre in SEZs; *(iii)* the public-private participation in infrastructure development; and *(iv)* the setting up of a "SEZ authority" in each central government SEZ for developing new infrastructure and strengthening the existing one.

Benefits of SEZs

- The promotion of SEZs is an attempt to deal with infrastructural deficiencies, procedural complexities, bureaucratic hassles and barriers raised by monetary, trade, fiscal, taxation, tariff and labour policies.
- Since country-wide development of infrastructure is expensive and implementation of structural reforms would require time, the establishment of SEZs is an important strategic tool for expediting the process of industrialization.
- SEZs offer numerous benefits like *(i)* tax incentives, *(ii)* provision of standard factories/plots at low rents with extended lease period, *(iii)* provision of infrastructure and utilities, *(iv)* single window clearance, *(v)* simplified procedures, and *(vi)* exemptions from various restrictions that characterize the investment climate in the domestic economy. These benefits foster a conducive business environment to attract local and foreign investment, which would not otherwise be forthcoming.
- SEZs are expected to give a big push to exports, employment and investment. The Ministry of Commerce claims that these zones are expected to attract investment of about Rs.1,00,000 crore including FDI of Rs.25,000 crore and create additional 5,00,000 direct jobs, by December 2007. It is said that if all the 234 SEZs approved till January 2007 become operational, investment of the order of Rs.3,00,000 crore may take place and 4 million additional jobs may be created.

Arguments against SEZs

- SEZ Act will lead to large-scale land acquisition by developers, displacement of farmers, meagre compensation and no alternative livelihood for them. The 234 SEZs given approval till January 2007 would require as much as 1,10,000 hectares of land.
- Currently, the government acquires land under an archaic Act of 1894, meant for public projects like the construction of roads or dams. However, under SEZ, the land is being taken by the State to benefit some particular private entities, i.e., for private profitability and not public good. While the State

governments claim that 'adequate compensation' is being paid, the question is 'what is adequate compensation'? Is it to be decided at current market rates or in terms of some future income foregone? For example, CPI (M) leader Sitaram Yechury reveals a shocking instance in Maharashtra where the government bought land from farmers at around Rs. 50,000 per hectare. After holding it for years, it has now sold it to a corporate for Rs. 62 lakh per hectare. This corporate, in turn, is now parcelling this land at Rs.10 crore per hectare to co-developers of its SEZ (see *India Today*, October 9, 2006, p. 59).

- SEZs will be built on prime agricultural land with serious implications for food security.
- Companies will simply re-locate to SEZs to take advantage of tax concessions being offered.
- There is a strong possibility that SEZs will be set up in States where there is already a strong tradition of manufacturing and exports. This will aggravate regional disparities.

EGoM Decision on SEZs

Following violent protest by farmers over the acquisition of their farmland in West Bengal and other States, the Government of India put a freeze on SEZs on January 22, 2007. This political freeze was lifted by the empowered group of Union Ministers (EGoM) on April 5, 2007. Decisions taken in this meeting were as follows:

- 83 SEZs cleared (total SEZs with formal approvals are 234).
- Upper limit on land for multi-product SEZs fixed at 5,000 hectares (State governments granted discretionary power to reduce the size of SEZs in their jurisdictions).
- Minimum share of processing area (i.e., area having manufacturing facilities) raised from 35 per cent to 50 per cent.
- States will no longer be able to compulsorily acquire land for SEZs under the Land Acquistion Act, barring zones they propose to set up on their own. Private developers will have to buy land directly from farmers and other owners.
- A comprehensive rehabilitation policy for people displaced by SEZs to be worked out. It would include a clause guaranteeing employment to at least one person from each displaced family in the corresponding economic zone.

Source: (*i*) Government of India, *Economic Survey*, 2006-07 (Delhi, 2007), Box 6.6, p,123: (*ii*) Aradhna Aggarwal, "Special Economic Zones: Revisiting the Policy Debate, "*Economic and Political Weekly*, November 4, 2006, pp.4533-6; (*iii*) Shankar Aiyar, "SEZ: Good, Bad, Ugly," *India Today*, October 9, 2006, pp,53-63: (*iv*) Puja Mehra, "SEZ Controversy: Course Correction," *India Today*, February 5, 2007, pp.54-55 and (*v*) *Business Standard*, April 6, 2007.

7. EOU scheme. The Export Oriented Units (EOUs) scheme introduced in early 1981, is complementary to the SEZ scheme. It offers a wide option in locations with reference to factors like source of raw materials, ports of export, hinterland facilities, and availability of technological skills, existence of an industrial base and the need for a larger area of land for the project. The EOUs have put up their own infrastructure. Exports by EOUs during 2004-05 were of Rs. 28,896 crore.

8. Agriculture Export Zones. The Exim Policy 2001 introduced the concept of Agri Export Zones (AEZs) to give primacy to promotion of agricultural exports and effect a reorganisation of our export efforts on the basis of *specific products* and *specific geographical areas.* The scheme is centred around the cluster approach of identifying the potential products, the geographical region in which these products are grown and adopting an end-to-end approach of integrating the entire process right from the stage of production till it reaches the market. The AEZs would have the state-of-the-art services such as pre-post harvest treatment and operations, plant protection, processing, packaging, storage and related research and development. The exporters in these zones can avail of the various export promotion schemes under the Exim Policy including recognition as a status holder.

9. Market Access Initiative Scheme. Market Access Initiative Scheme was launched in 2001-02 for undertaking marketing promotion efforts abroad. The key features of the scheme are in-depth Market Studies for select products in chosen countries to generate data for promotion of exports from India, assist in promotion of India, Indian products and Indian brands in the international market by display through showrooms and warehouses set up in rental premises by identified exporters, display in identified leading departmental stores/ trade exhibitions/trade fairs, etc. The scheme shall also assist quality upgradation of products as per requirements of overseas markets, intensive publicity campaigns, etc.

10. Focus on Service Exports. The Amended Export-Import Policy, 2002-07, announced on March 31, 2003, specifically emphasized service exports as an engine of growth. It, accordingly, announced a number of measures for the promotion of exports of services. For instance, import of consumables, office and professional equipment, spares and furniture upto 10 per cent of the average foreign exchange export earning during the last three years, has been allowed. The advance licence system has been extended to the tourism sector. Under this, firms will be allowed duty free import of consumables and spares upto 5 per cent of their average foreign exchange earnings of the previous three years, subject to actual user condition.

11. Concessions and Exemptions. A large number of tax benefits and exemptions have been granted during the 1990s to liberalise imports and promote exports with the five year Exim Policy 1992-97 and Exim Policy 1997-2002 serving as the basis for such concessions. These policies, in turn, have been reviewed and

modified on an annual basis in the Exim policies announced every year. Successive annual Union Budgets have also extended a number of tax benefits and exemptions to the exporters. These include reduction in the peak rate of customs duty to 10 per cent; significant reduction in duty rates for critical inputs for the Information Technology sector, which is an important export sector; grant of concessions for building infrastructure by way of 10-years tax holiday to the developers of SEZs; facilities and tax benefits to exporters of goods and merchandise; reduction in the customs duty on specified equipment for Ports and Airports to 10 per cent to encourage the development of world class infrastructure facilities, etc. A number of tax benefits have also been announced for the three integral parts of the 'convergence revolution' — the Information Technology sector, the Telecommunication sector, and the Entertainment industry.

A Critical Evaluation of the New Trade Policy[10]

The trade policy reforms initiated in 1991 have drastically changed the foreign trade scenario and have resulted in the shift from inward-oriented to an outward-oriented policy. With the sweeping liberalisation process that is currently underway in the foreign trade sector, the level of protection to Indian industry has declined significantly as the government has resorted to a massive cutting down of import tariffs and allowing more liberal imports of a number of goods whose imports were earlier either totally banned or severely restricted. The euphoria and enthusiasm generated by the large-scale trade policy reforms in recent years and talks of globalisation etc. have led many in the official and non-official circles to regard the foreign trade sector in India now as the 'leading sector' of the economy — a sector that will change the face of the economy in the coming years giving it a strong push up in the world economy. However, in this euphoria, one should not ignore the following three issues which, according to Deepak Nayyar, are of fundamental or strategic importance in planning for industrialisation — the relative importance of the home market, the nature or the degree of State intervention, and the acquisition or development of technology.

1. Relative importance of the home market. As far as the issue of the relative importance of the home market is concerned, Deepak Nayyar argues that in large countries like India, where the domestic market is overwhelmingly important, sustained industrialisation can only be based on the growth of the internal market.[11] In the ultimate analysis, ***large economies must endeavour to internalise external markets.*** Therefore, industrialisation may stress manufacturing for the domestic market through import substitution or manufacturing for export to external markets. "In terms of an appropriate strategy for industrialization, striking a balance between import substitution and export promotion is the equivalent of 'walking on two legs.'... An environment that produces a spectacular export performance is also conducive to efficient import substitution and rapid economic growth."[12]

2. The nature or the degree of State intervention. As far as the issue of State intervention in the process of industrialization is concerned, the experience of the second half of the twentieth century shows that the guiding and supportive role of the State has been at the foundation of successful development among the late industrialisers. This is true not only in the case of the centrally planned economies of Eastern Europe but also in the case of the market economies of East Asia. According to Deepak Nayyar, in terms of State intervention, there is not much to distinguish between import substitution and export promotion. In the former, the State protects the domestic capitalists from foreign competition in the home market while in the latter, the State protects the domestic capitalists from foreign competition in the world market. It is the 'nature' of State intervention that matters. It is this nature and degree of State intervention in the foreign trade sector that deserves serious attention in the context of planning for industrialisation.

3. The issue of technology. As far as the issue of technology is concerned, Nayyar argues that the existing market structure and policy framework have not combined to provide an environment that could accelerate the absorption of imported technology and foster the development of indigenous technology, or create a milieu which could be conducive to diffusion and innovation. It needs to be stressed that the role of the government is crucial in planning for technological development across sectors and over time. This requires the formulation of policy regime for the import of technology (planning for the acquisition of technology, taking steps for its absorption, adaptation, diffusion etc.), allocating resources for research and development, and evolving State procurement policies.[13]

The above discussion points out the vital fact that the ***'macro-economic interconnections' between the foreign trade sector and the overll process of planning for industrialization are crucial.*** The solutions to the problems of the national economy cannot be found through the foreign trade sector or simple recipes associated with it. On the other hand, the problems of the foreign trade sector can be resolved to a considerable extent, through an improved performance and a better management of the economy at home. "In other words, the tail cannot wag the dog."[14]

FOREIGN TRADE POLICY (2004-09)

The Central government announced a new foreign trade policy (FTP) covering the period 2004 to 2009 on August 31, 2004. We present below the main features of this policy and its critical evaluation.

Main Features of FTP, 2004-09

The main features of FTP, 2004-09, are as follows:

1. Doubling share of global merchandise trade. FTP (2004-09) envisages a doubling of India's share in world exports from 0.75 per cent to 1.5 per cent by 2009.

2. Five thrust sectors. Sectors with significant export prospects coupled with potential for employment generation in semi-urban and rural areas were identified as thrust sectors. ***FTP announced specific strategies (termed 'Special Focus Initiatives') for five sectors: Agriculture, Handicrafts, Handlooms, Gems & Jewellery, and Leather and Footwear sector.***

Main strategies announced for the five sectors outlined in the FTP are as follows:

- In agriculture, a new scheme called ***Vishesh Krishi Upaj Yojana*** was introduced to boost exports of fruits, vegetables, flowers, minor forest produce and their value added products. Export of these products would qualify for duty free credit entitlement equivalent to 5 per cent of the value of exports. In addition, the policy made capital goods imported for agriculture under the Export Promotion Capital Goods (EPCG) scheme duty free.
- The package for gems and jewellery sector includes *(i)* duty free import of consumables for metals other than gold and platinum up to 2 per cent of the value of exports; *(ii)* duty free re-import entitlement for rejected jewellery upto 2 per cent of the value of exports; *(ii/)* duty free import of commercial samples of jewellery. increased to Rs. 1 lakh; and *(iv)* allowing import of gold of 18 carat and above under the replenishment scheme.
- As far as the handlooms and handicrafts sector is concerned, the FTP announced that a new Handicraft Special Economic Zone would be established. In addition, duty sops for trimmings and embellishments imported by handlooms and handicraft producers were increased to 5 per cent of the value of exports.
- In the leather and footwear sector, the duty-free entitlements of import trimmings, embellishments and footwear components were increased to 3 per cent. This is expected to help the leather and footwear sector save up to 5 per cent of its import costs. In addition, duty free import of specified items for leather sector was increased to 5 per cent of the value of exports.

3. 'Served from India' to be built as a brand. Presently services contribute more than 50 per cent of the country's GDP. To provide a thrust to service exports, FTP advocated a number of steps. These include:

- **Served from India** brand will be created to catapult India the world over as a major global services hub.
- An exclusive Export Promotion Council for services would be set up in order to map opportunities in key markets, and develop strategic market access programmes.
- Individual service providers who earn foreign exchange of at least Rs. 5 lakh, and other service providers who earn foreign exchange of at least Rs. 10 lakh would be eligible for a duty credit entitlement of 10 per cent of total foreign exchange earned by them.
- Stand-alone restaurants would be entitled to duty credit equivalent to 20 per cent of the foreign exchange earned. In the case of hotels, the entitlement would be 5 per cent.
- Healthcare and educational institutions would be entitled to duty credit of 10 per cent of the foreign exchange earned.

4. New categories of star houses. The FTP announced a new categorisation of status holders. Under the new scheme, export houses were divided into five categories depending upon their export performance. The categories are as under :

Category	*Export Performance in three years*
1 star	Rs. 15 crore
2 star	Rs. 100 crore
3 star	Rs. 500 crore

4 star	Rs. 1,500 crore
5 star	Rs. 5,000 crore

A star export house would be entitled to get licence, certificate, permissions and customs clearances for both imports and exports on self-declaration basis. The star export house would get the benefit of 100 per cent retention of foreign exchange in Export Earner's Foreign Currency (EEFC) account. It would also be eligible for consideration under the Target Plus Scheme and enjoy a number of other privileges (like exemption from furnishing Bank Guarantee).

5. 'Target Plus' Scheme. Exporters who exceed the annual export target were to be rewarded under the ***Target Plus Scheme***. This reward was in terms of entitlement to duty-free credit based on incremental export earnings. With the target for 2004-05 being fixed at 16 per cent, the lower limit for qualifying for these rewards was pegged at 20 per cent. Target Plus Scheme was abandoned in the second supplement to Foreign Trade Policy announced on April 7, 2006.

6. Setting up of Free Trade and Warehousing Zones (FTWZs). The FTP introduced a new scheme to establish Free Trade and Warehoushing Zones (FTWZs) to create trade-related infrastructure to facilitate the import and export of goods and services with freedom to carry out trade transactions in free currency. This is aimed at making India into a global trading hub. Each zone would have minimum outlay of Rs. 100 crore and 5,00,000 square metres built-up area. Foreign direct investment would be permitted upto 100 per cent in the development and establishment of the zones and their infrastructural facilities.

7. Sops for EOUs. The FTP announced a number of benefits for the export-oriented units (EOUs). These include: (*i*) EOUs to be exempted from service-tax in proportion to their exported goods and services; (*ii*) EOUs to be permitted to retain 100 per cent of export earnings in EEFC accounts; (*iii*) Income tax benefits on plant and machinery to be extended to DTA (Domestic Tariff Areas) that convert into EOUs; and (*iv*) Import of capital goods to be on self-certification basis for EOUs.

8. Reducing transactional costs and simplifying procedures. The FTP announced a number of 'rationalization measures' to reduce transactional costs and simplify procedures. These inculde: (*i*) All exporters with a minimum turnover of Rs. 5 crore exempted from funishing bank guarantee (this will help small exporters who incur high transactional costs); (*ii*) Import of second hand capital goods permitted without any age restrictions; (*iii*) Minimum depreciated value for plant and machinery to be relocated into India reduced from Rs. 50 crore to Rs. 25 crore; (*iv*) All goods and services exported, including those from DTA units, exempted from service tax (this will further reduce costs and enable Indian exports to compete with countries in Southeast Asia and China); (*v*) Validity of all licences and entitlements issued under various schemes increased to a uniform 24 months; (*vi*) The number of returns and forms to be filed reduced; (*vii*) Time bound introduction of Electronic Data Interface (EDI) for export transactions, etc.

9. Focus on Infrastructure Development. Some special measures announced for infrastructure development in the FTP are: (*i*) The threshold limit of designated 'Towns of Export Excellence' has been reduced from Rs. 1,000 crore to Rs. 250 crore in the five thrust-sectors announced; (*ii*) Funds from ASIDE (Assistance to States for Infrastructure Development of Exports) would now be used for development of Agri Export Zones also; (*iii*) Establishment of Common Facility Centres will be encouraged for use by house-based service providers; and (*iv*) Pragati Maidan at Delhi will be transformed into a world-class complex.

10. Other measures. Of the various other measures announced in the FTP, the following deserve specific mention : (*i*) Biotechnology Parks to be set up in the country having all the facilities of 100 per cent EOUs; (*ii*) The Board of Trade to be revamped and given a clear and dynamic role; and (*iii*) Financial assistance to be provided to exporters for meeting their costs and legal expenses related to trade matters like anti-dumping action and countervailing duties in other countries.

A Critical Evaluation of FTP

As the discussion above shows, the Foreign Trade Policy, 2004-09 introduced a number of schemes for promoting exports and opening up trade. However, it has been criticized on a number of counts. The main criticisms are as follows :

1. Burden of export promotion schemes. The various export promotion schemes have resulted in a substantial loss of revenue to the government. This loss was Rs. 37,590 crore in 2005-06 and is estimated to have touched the figure of Rs. 53,768 crore in 2006-07.[15] It is difficult to appreciate the plethora of liberal giveaways to the various categories of exporters like duty free entitlements for status holders, service providers

and agri-exporters and easier status recognition norms. While the FTP has announced a number of concessions and exemptions, it says nothing on business or businessmen who avail of duty exemptions but do not fulfill their obligations. "In practice, the government has given whoever masquerades as exporter, complete freedom to evade duties through export promotion licences."[16]

2. Danger of circular trading. At the time FTP, 2004-09, was announced, some critics had expressed the apprehension that the target plus scheme could lead to a sharp rise in 'circular trading' in the guise of increasing exports. This is due to the reason that the scheme had given incentives for achieving higher exports without any linkage to the volume of imports. For instance, suppose that an exporter, with a turnover of Rs. 500 crore in 2003-04, imported inputs worth Rs. 1,000 crore in 2004-05. He could claim credit for 100 per cent export growth by re-exporting the imported goods even with a nominal value addition. Under the target plus scheme, the exporter would then be eligible for an incentive of upto 15 per cent on the incremental value of his exports (for 100 per cent incremental export growth, the incentive was 15 per cent). This would translate into a reward of Rs. 75 crore (15 per cent of Rs. 500 crore) on a nominal value addition. Thus, the Target Plus Scheme carried the danger of circular trading. This could create problems for the government in the long run.

The actual working of the Target Plus Scheme showed that the above criticism was correct as it led to a substantial revenue leakage. Accordingly, ***the government abondoned this scheme in the second supplement of FTP announced on April 7, 2006.***

3. Risk of importing outdated machinery. The FTP allowed the import of second-hand machinery without any age limit. This might result in the import of very old machines from the Western countries which could be outdated and dilapidated. Import of such machinery can become a burden on the economy. In any case, it is not likely to help exports at all.

4. Policy fails to take a holistic view of trade issues. The most important criticism of the FTP is that it fails to take a holistic view of the issues and concerns intricately connected with foreign trade or draw up a clearer road map to achieve the targeted export growth. As correctly pointed out by TNC Rajagopalan, ***the FTP says next to nothing about the government's negotiating stance at the WTO, trade relations with neighbours, approach towards bilateral trade agreements, integration of development and globalisation strategies, helping market penetration, market access issues, competitiveness, project exports and so on.***[17]

Third Supplement to FTP Announced in April 2007

The First Supplement to FTP, 2004-09, released on April 18, 2005 kept the export target for 2005-06 at $ 92 billion which was exceeded as the exports touched the level of $ 103 billion in this year. The Second Supplement to FTP, 2004-09, released on April 7, 2006 kept the export target for the year 2006-07 at $ 120 billion which was again exceeded as the exports touched the level of $ 125 billion. Since exports were $ 63.84 billion in 2003-04, this means that ***exports have almost doubled during this three year period. This implies an annual compounded growth of 25 per cent compared to 12.73 per cent in the previous three years.*** Emboldened by this, the Third Supplement to FTP, 2004-09, released on April 19, 2007 has set the export target for the year 2007-08 at $ 160 billion. The highlights of the Third Supplement are presented in Box 28.2.

Issues of Concern. As stated above, the exports have shown a remarkable buoyancy in the past three years and have doubled indicating a robust 25 per cent compounded annual increase during this period. However, there are certain issues of concern :

1. While exports have increased rapidily, imports have risen at a still faster rate with the result that trade deficit is increasing fast. ***The trade deficit touched $ 46.07 billion in 2005-06 and rose further to $ 57 billion in 2006-07*** (as imports crossed $ 180 billion). While exports are targeted to increase to $ 160 billion in 2007-08, imports are likely to touch $ 223 billion. Thus, ***trade deficit is likely to increase further to $ 63 billion in 2007-08.***

2. The export target of $ 160 billion in 2007-08 is based on the assumption that the rupee depreciates to Rs. 43 to a dollar. However, the rupee has been actually appreciating against the dollar and the rate on January 18, 2008 was Rs. 39.30 to a dollar.

3. The export growth has been achieved at a considerable cost to the exchequer. As stated earlier, the revenue foregone on account of export promotion schemes was as high as Rs. 37,590 crore in 2005-06 and is estimated to have touched the figure of Rs. 53,768 crore in 2006-07.

BOX 28.2. Third Supplement to FTP, 2004-09 (Announced in April 2007)

- **Export target:** 28 per cent growth target, i.e., a target of $160 billion in 2007-08.
- **No service tax on exports:** Service tax on export of goods and services removed (which was levied at the rate of 12.24 per cent on exports from India).
- **New status holder scheme:** The status holder scheme has been revamped. Under the scheme to classify exporters, the categories have been re-christened an Export House (earlier known as One Star Export House), Star Export House (earlier known as Two Star Export House), Trading House (earlier known as Three Star Export House), Star Trading House (earlier known as Four Star Export House) and Premier Trading House (earlier known as Five Star Trading House). The exporters will be granted such status on achieving aggregate exports of Rs. 20 crore, Rs. 100 crore, Rs. 500 crore, Rs. 2,500 crore and Rs. 10,000 crore over four years.
- **Focus Market Scheme extended:** Focus market programme which covers 57 countries has been extended to include 16 more countries (which includes 10 central Asian economies formerly with the Soviet Union). Under the programme, exporters can claim duty concessions totaling 2.5 per cent of the value of exports to these countries.
- **Focus Product Scheme:** Buoyed by the success of the Focus Product Scheme, mica and its variants, barley, oats, soyabean, cigar and cheroots, bovine fats and copra included under it. Total allocation for the Focus Market and Focus Product scheme increased to Rs. 1,000 crore from Rs. 650 crore.
- **Scope of VKGUY expanded:** To boost exports of farm products from India, the scope of the Vishesh Krishi and Gram Udyog Yojana expanded to include exports of value-added variants of several agricultural and forest products, including coconut oil, soyabean oil, potato flakes, meals and flour. Exporters can avail duty credit equivalent to 5 per cent of the freight on board value of notified items under this scheme.
- **Two new export promotion schemes launched:** Two new export promotion schemes incentivising hi-tech exports and agro-processing launched. The new scheme on hi-tech exports envisages a duty credit of 10 per cent on incremental export growth to the exporter subject to a ceiling of Rs. 15 crore for each firm.

  In order to give incentives to the agro-processing sector, a new export promotion scheme has been unveiled under which duty credit equal to 10 per cent of the value of agricultural exports will be provided for duty redemption on imports of cold storage, pack houses and reefer vans.
- **DEPB extended:** The Duty Entitlement Pass Book Scheme (DEPB) extended till March 31, 2008 —to be replaced by a new scheme by next year.
- **Credit to Small and Medium Enterprises:** Commercial banks are required to lend 15 per cent of their total credit to export-oriented undertakings. It has been observed that most banks meet the criteria by lending to a handful of large undertakings. It was, accordingly, proposed to request the Reserve Bank to ensure that about 50 per cent of the total credit to exporters is given to small and medium enterprises.
- **Period under EPCG extended:** The tiny and cottage industry, which has been adversely hit by the rupee's appreciation, has been given 12 years to complete its export obligations instead of the normal 8 years.
- **Sops for SEZ investors:** The developer and the co-developer of the special economic zones (SEZs) would be entitled to all-duty exemption and remission schemes like the advance authorization scheme, and DEPB and Duty Free Import Authorisation.

NOTES

1. Suresh D. Tendulkar and T.A. Bhavani, *Understanding Reforms : Post 1991 India* (New Delhi, 2007), p. 33.
2. T.N. Srinivasan, "Foreign Trade Policies and India's Development", in Uma Kapila (ed.), *Indian Economy Since Independence* (New Delhi, 2003), p. 665.
3. Jagdish Bhagwati and Padma Desai, *India-Planning for Industrialization* (London, 1970), p. 312.
4. T.N. Srinivasan, "Foreign Trade Polices and India's Development", *op.cit.,*
5. Jaleel Ahmed, "Foreign Trade and Balance of Payments," in J.S. Uppal (ed.), *India's Economic Problems* (New Delhi, 1987), p. 501.
6. Deepak Nayyar, "India's Export Performance, 1970-85," *Economic and Political Weekly,* Annual Number, 1987, p. 81.
7. *Ibid.,* Table 2, p. 74. Also see p. 75.
8. Bimal Jalan, "Balance of Payments, 1956-1991," in Bimal Jalan (ed.), *The Indian Economy: Problems and Prospects* (New Delhi, Revised edition, 2004), p. 200.
9. T.N. Srinivasan, *op.cit.*, pp. 673-4.
10. In this context, please also see the section on 'Growth and Structural Change of India's Foreign Trade Sector Since 1991' of chapter 41.
11. Deepak Nayyar, "The Foreign Trade Sector, Planning and Industrialisation in India," in Thomas J. Byres (ed), *The State, Development Planning and Liberalisation in India* (Delhi, 1997), p. 360.
12. *Ibid.*, pp. 360-1.
13. *Ibid.*, p. 362.
14. *Ibid.*, p. 362.
15. *Business Standard,* April 20, 2007, p. 10.
16. Comment on Foreign Trade Policy, 2004-09, by TNC Rajagopalan in *Business Standard,* Special Supplement, Sept. 1, 2004, p. 10.
17. *Ibid.,* p. 10.

CHAPTER

29

FERA AND FEMA

Foreign Exchange Regulation Act (FERA), 1973
• Objectives of FERA • Restrictive Provisions of FERA • Provisions Relating to Enforcement • Penalty and Prosecution
Foreign Exchange Management Act
• Regulation and Management of Foreign Exchange • Authorised Person • Contravention and Penalties • Adjudication and Appeal • Directorate of Enforcement • Miscellaneous
FEMA: A Major Departure from FERA

Foreign exchange transactions have traditionally been regulated in India. For this purpose, Foreign Exchange Regulation Act (FERA) was promulgated in 1973. However, with recent trends of liberalisation in the economy, the focus has shifted from regulation to management with the result that FERA has been replaced by FEMA (Foreign Exchange Management Act). In this chapter, we propose to discuss:

- FERA and its provisions
- FEMA and its provisions
- Differences between FERA and FEMA.

FOREIGN EXCHANGE REGULATION ACT (FERA), 1973

Foreign Exchange Regulation Act (FERA) was promulgated in 1973 and it came into force on January 1, 1974. As the name of the Act itself implies, ***the Act aimed at regulating foreign exchange.***

Objectives of FERA

The main objectives of FERA were as under:

1. To regulate certain payments.
2. To regulate dealings in foreign exchange and securities.
3. To regulate transactions indirectly affecting foreign exchange.
4. To regulate the import and export of currency.[1]
5. To conserve the foreign exchange resources of the country and to ensure their proper utilisation in the interests of the economic development of the country.
6. To regulate the acquisition, holding, transfer or disposal of immovable property abroad by persons resident in India (other than foreign nationals).
7. To regulate participation by residents in India in the trading, commercial and industrial activities abroad in the form of joint ventures.
8. To regulate the appointment of agent or technical or management adviser of any person or company in foreign companies (defined as companies incorporated outside India or in which the non-resident interest is more than 40 per cent).

9. To regulate the purchase of goods in India (with a view to reselling them before processing) by foreign companies.
10. To regulate foreign investment in the form of branches in India so that prior permission of Reserve Bank is required by foreign companies to carry on in India, or establish a branch/office or other place of business in the country for carrying on any activity of a trading, commercial or industrial nature.
11. To regulate employment of foreign nationals.
12. To regulate the acquisition etc. of immovable property in India by foreign nationals or foreign companies.

Restrictive Provisions of FERA

The main provisions of FERA, 1973 as amended in 1993, are as follows:

Restrictions on Dealing in Foreign Exchange. Under the provisions of the Act, Reserve Bank of India is the sole authority to regulate foreign exchange transactions. Section 8 of the Act laid down that no person other than an authorised dealer, shall deal in foreign exchange or enter into any transactions involving foreign exchange without the prior permission of the Reserve Bank.

Restrictions on Payments. Section 9 laid down certain restrictions on payments. It provided that, unless authorised by the Reserve Bank, no person in India shall :

(*a*) make any payment to or for the credit of any person resident outside India;
(*b*) receive, otherwise than through an authorised dealer any payment by order or on behalf of any person resident outside India;
(*c*) draw, issue or negotiate any bill of exchange or promissory note or acknowledge any debt, so that a right (whether actual or contingent) to receive a payment is created or transferred in favour of any person resident outside India;
(*d*) make any payment to, or for the credit of, any person by order or on behalf of any person resident outside India;
(*e*) place any sum to the credit of any person outside India;
(*f*) make any payment to, or for the credit of, any person or receive any payment for, or by order or on behalf of any person as consideration for or in association with—
    (*i*) the receipt by any person of a payment or the acquisition by any person of property outside India;
    (*ii*) the creation or transfer in favour of any person of a right (whether actual or contingent) to receive payment or acquire property outside India;
(*g*) draw, issue or negotiate any bill of exchange or promissory note, transfer any security or acknowledge any debt, so that a right (whether actual or contingent) to receive a payment is created or transferred in favour of any person as consideration for or in association with any matter referred to in clause (*f*).

Restriction on Import and Export of Certain Currency and Bullion. Section 13 of the Act provided that except with the permission of the Reserve Bank, no person can bring or send into India any foreign exchange or any Indian currency other than foreign exchange obtained by him from an authorised dealer or from a money-changer (prior to 1993, no person could, without the permission of Reserve Bank, bring or send gold or silver as well but this condition was omitted by the Foreign Exchange (Amendment) Act, 1993).

The implication of the above section is that if any person had foreign exchange without the authorisation/permission of the Reserve Bank, that foreign exchange had to be offered for sale to the Reserve Bank (or to such person, as the Reserve Bank may authorise for the purpose) at a price fixed by the Central Government.

Duty of Persons Entitled to Receive Foreign Exchange. Section 16 of the Act provided that no person who has a right to receive any foreign exchange or to receive from a person resident outside India a payment in rupees shall, except with the permission of the Reserve Bank, do anything which has the effect of securing—

(*a*) that the receipt by him of the whole or part of that foreign exchange or payment is delayed, or
(*b*) that the foreign exchange or payment ceases in whole or in part to be receivable by him.

Payment for Exported Goods. Section 18 provided that the Central Government may, by notification in the official Gazette, prohibit the export of goods from India to any place so specified unless the exporter furnishes to the prescribed authority a declaration in the prescribed form all particulars relating to the full export value of goods and affirms in the said declaration that the full export value of the goods (whether ascertainable at the time of export or not) has been, or will within the prescribed period be, paid in the prescribed manner. The Central Government may, by notification, specify that goods cannot be sold at a value less than that declared by the exporter except with the permission of the Reserve Bank.

Regulation of Export and Transfer of Securities. Section 19 of the Act provided that no person shall,

except with the permission of the Reserve Bank, transfer or send any security to any place outside India; transfer any security, or create or transfer any interest in a security, to or in favour of a person resident outside India; issue any security which is registered in India to a person outside India; and acquire, hold or dispose of any foreign security.

Restrictions on Holding of Immovable Property Outside India. Section 25 of the Act laid down that no person, resident in India shall, except with the permission of the Reserve Bank, acquire or hold or transfer or dispose of by sale, mortgage, lease, gift, settlement, or otherwise, any immovable property outside India (excepting the acquisition or transfer of any such immovable property by way of lease for a period not exceeding five years). The section does not apply to a national of a foreign State.

Restriction on Acquisition, Holding etc. of Immovable Property in India. Sub-section 1 of Section 31 of the Act laid down that no person who is not a citizen of India and no company (other than a banking company) which is not incorporated under any law in force in India shall, except with the permission of the Reserve Bank, acquire or hold or transfer or dispose of by sale, mortgage, lease, gift, settlement or otherwise any immovable property in India (excepting the acquisition or transfer of any such immovable property by way of lease for a period not exceeding five years).

Sub-section 2 of Section 31 laid down that any person or company referred to in sub-section (1) can acquire immovable property in India provided it makes application to the Reserve Bank in this regard in the prescribed form (and containing all particulars as required by the Reserve Bank) and provided that the Reserve Bank grants permission after an examination of his/its application.

Restrictions on Appointment of Certain Persons and Companies as Agents or Technical or Management Advisers in India. Section 28 of the Act laid down that a person resident outside India (whether a citizen of India or not) or a person who is not a citizen of India but is resident in India, or a company (other than a banking company) which is not incorporated under any law in force in India or any branch of such company, shall not, except with the permission of the Reserve Bank, act, or accept appointment, as agent in India of any person or company, in the trading or commercial transactions of such person or company. Sub-section 2 of Section 28 laid down that where any such person or company acts or accepts appointment as such agent without the permission of the Reserve Bank, such acting or appointment shall be void.

Restrictions on Establishment of Place of Business in India. Section 29 of the Act laid down that a person resident outside India (whether a citizen of India or not) or a person who is a not a citizen of India but is resident in India, or a company (other than a banking company) which is not incorporated under any law in force in India or any branch of such company, shall not, except with the permission of the Reserve Bank—

(*a*) carry on in India, or establish in India a branch, office or other place of business for carrying on any activity of a trading, commercial or industrial nature, other than an activity for the carrying on of which permission of the Reserve Bank has been obtained under Section 28; or

(*b*) acquire the whole or any part of any undertaking in India of any person or company carrying on any trade, commerce or industry or purchase the shares in India of any such company.

Sub-section 2 of Section 29 laid down that if any person or company referred to above has established an office or other place of activity, that person or company may make an application to the Reserve Bank within a period of six months from such commencement (or such further period as the Reserve Bank may allow) for permission to continue to carry on such activity. The Reserve Bank, after making such enquiry as it may deem fit, may either allow the application or reject it. In the latter case, the person or company concerned shall discontinue its activity or close down the branch, office or other place of business established for carrying on such activity, on the expiry of a period of ninety days (or such other later date as may be specified by the Reserve Bank).

Prior Permission for Taking up Employment, etc. in India by Nationals of Foreign States. Section 30 of the Act laid down that no national of a foreign State shall, without the previous permission of the Reserve Bank, practice any profession or carry on any occupation, trade or business in India in a case where such national desires to acquire any foreign exchange (such foreign exchange being intended for remittance outside India) out of any moneys received by him in India by reason of the practising of such profession or the carrying on of such occupation, trade or business, as the case may be.

Provisions Relating to Enforcement, Penalty and Prosecution

Sections Dealing With Enforcement. Section 33 laid down that the Central Government may, at any time by notification, direct the owners to submit returns regarding their transactions in foreign exchange or foreign

securities or immovable properties outside India. Section 34 dealt with the power conferred on the officers of Enforcement to search suspected persons and to seize documents; Section 35 with the power to arrest persons guilty of an offence punishable under the Act; Section 36 with the power to search conveyances; Section 37 with the power to search premises; Section 38 with the power to seize documents, etc.; Section 39 with power to examine persons; Section 40 with power to summon persons to give evidence and produce documents; Section 41 with custody of documents etc.; Section 42 with encashment of cheque, draft etc.; Section 43 with inspection of the books and accounts and other documents of any authorised dealer; Section 44 with prohibition of disclosure of documents or information except in certain cases; Section 45 with the power of police officers and other officers to enter, search etc.; and Section 46 with procedure in respect of foreign exchange or any other goods seized by police officers.

Penalty, Adjudication and Appeal. Section 50 laid down that if any person contravenes any of the provisions of the Act or of any rule, direction or order made thereunder, he shall be liable to such penalty not exceeding five times the amount or value involved in any such contravention or five thousand rupees, whichever is more, as may be adjudged by the adjudicating officer. Section 51 deals with the power of the adjudicating officer to impose penalty. Section 52 related to the constitution of the Appellate Board consisting of a chairman and such number of other members, not exceeding four to be appointed by the Central Government for hearing appeals against the order of the adjudicating officer made under Section 51. Section 53 was concerned with the powers of the adjudicating officer and the Appellate Board to summon witnesses etc.

Offences and Prosecutions. Section 56 laid down that if any person contravenes the provisions of the Act, he shall, upon conviction by a court, be punishable: (*i*) in the case of an offence the amount or value involved in which exceeds one lakh of rupees, with imprisonment ranging from six months up to seven years and with fine; (*ii*) in any other case, with imprisonment extending to three years or with fine or with both. Section 57 laid down that if a person fails to comply with such directions or orders, he shall, upon conviction by a court, be punishable with imprisonment for up to two years or with fine or with both.

FOREIGN EXCHANGE MANAGEMENT ACT (FEMA)

As shown by the list of objectives of FERA and the provisions of FERA stated above, the entire focus of this Act was on regulating all transactions and dealings in foreign exchange and imposing restrictions on foreign companies. This was resented to both by champions of the big industry and the foreign investors. After the new industrial and trade policy was announced in 1991, the government itself felt that there was a dire need to simplify regulations relating to foreign investment, remove special restrictions in respect of companies registered in India and delete redundant provisions of FERA in order to attract better inflow of foreign capital and investment. Thus important steps were taken to reduce the rigours of FERA through certain notifications issued by the Reserve Bank of India. Various facilities were extended to foreign/FERA companies on the appointment of technical and management advisors, opening of branches, acquisition of immovable property, borrowing of money or acceptance of deposits, etc.. 51 per cent foreign subsidiaries in a few 'priority industries' were brought under automatic approval and thus, in effect, freed from import licensing. Facilities were also extended to non-resident Indians (NRIs), Indian companies and residents for the opening of foreign currency accounts in India following the introduction of partial convertibility of rupee on the current account since March 1, 1992. Notifications were also issued exempting NRIs returning to the country from making declarations on their arrival in India regarding their assets abroad and from the requirement of prior approval for the acquisition of immovable property in India. The Government of India also amended the FERA in 1993 with a view to : (*a*) incorporate into the law all the changes which have been made by issue of notifications by the Reserve Bank/Central Government in order to give assurance of their permanence; (*b*) delete Sections which have lost their relevance over time; and (*c*) rationalise other Sections which are considered necessary but should be amended to do away with the rigours or irrationalities experienced while administering the Act. As a result of the Foreign Exchange Regulation (Amendment) Act, 1993, a number of restrictions of FERA, 1973, were either dropped or substantially diluted with a view to encouraging foreign investment in the country. Sections of FERA, 1973, which were deleted, revoked, amended or diluted by the Amendment Act included Sections 11, 12, 13, 15, 17, 19, 20, 21, 22, 23, 25, 26, 27, 28, 29, 30, 31 and 32. As a result of these deletions, amendments etc., the foreign companies received considerable incentives and concessions to extend their operations in India.[2]

However, despite the above concessions and liberalisation, the private sector and foreign investors kept up pressure on the government for repealing of FERA as they still felt that it was excessively restrictive. The

government itself concurred with this view as is clear from the following statement made by the Finance Minister while introducing Foreign Exchange Management Bill (FEMA), "Significant developments have taken place since 1993 such as substantial increase in our foreign exchange reserves, growth in foreign trade, rationalisation of tariffs, current account convertibility, liberalisation of Indian investments abroad, increased access to external commercial borrowings by Indian corporates and participation of foreign institutional investors in our stock market."[3] Therefore, the Central Government decided to introduce the Foreign Exchange Management Bill (FEMA) and repeal the Foreign Exchange Regulation Act, 1973. FEMA was introduced by the Finance Minister in the Lok Sabha on August 4, 1998. The Bill aimed ***"to consolidate and amend the law relating to foreign exchange with the objective of facilitating external trade and payments and for promoting the orderly development and maintenance of foreign exchange market in India."*** It was adopted by the Parliament in 1999 and is known as the Foreign Exchange Management Act, 1999. This Act extends to the whole of India and shall also apply to all branches, offices and agencies outside India owned or controlled by a person resident in India.

Regulation and Management of Foreign Exchange

Chapter II of the Act deals with the regulation and management of foreign exchange. Section 3 states that except as otherwise provided in this Act, no person shall in any manner deal in or transfer any foreign exchange or foreign security to any person not being an authorised person. Section 4 states that except as otherwise provided in this Act, no person resident in India shall acquire, hold, own, possess or transfer any foreign exchange, foreign security or any immovable property situated outside India.

Current Account and Capital Account Transactions. Sections 5 and 6 deal with current and capital account transactions. According to Section 5, any person may sell or draw foreign exchange to or from an authorised person if such sale or drawal is a current account transaction. However, the Central Government may, in public interest and in consultation with the Reserve Bank, impose such reasonable restrictions for current account transactions as may be prescribed. According to Sub-section 1 of Section 6, any person may sell or draw foreign exchange to or from an authorised person for a capital account transaction subject to provisions of Sub-section 2. Sub-section 2 states that Reserve Bank may, in consultation with the Central Government, specify : (*a*) any class or classes of capital account transactions which are permissible; (*b*) the limit up to which foreign exchange shall be admissible for such transactions. However, the Reserve Bank shall not impose any restriction on the drawal of foreign exchange for payments due on account of amortization of loans or for depreciation of direct investments in the ordinary course of business.

Export of Goods and Services. Sub-section 1 of Section 7 of the Act lays down that every exporter of goods shall—

(*a*) furnish to the Reserve Bank or to such other authority a declaration in such form and in such manner as may be specified, containing true and correct material particulars, including the amount representing the full export value (or if the full value is not ascertainable at the time of export, the value which the exporter expects to receive);

(*b*) furnish to the Reserve Bank such other information as may be required by the Reserve Bank for the purpose of ensuring the realisation of export proceeds by such exporter.

Realisation and Repatriation of Foreign Exchange. Section 8 lays down that save as otherwise provided in the Act, where any amount of foreign exchange is due or has accrued to any person resident in India such person shall take all reasonable steps to realise and repatriate to India such foreign exchange within such period and in such manner as may be specified by the Reserve Bank.

Section 9 provides the following exemptions from realisation and repatriation of foreign exchange: (*a*) possession of foreign currency or foreign coins by any person upto such limit as the Reserve Bank may specify; (*b*) foreign currency account held or operated by such person or class of persons and the limit up to which the Reserve Bank may specify; (*c*) foreign exchange acquired or received before the 8th day of July, 1947 or any income arising or accruing thereon which is held outside India by any person in pursuance of permission granted by the Reserve Bank; (*d*) foreign exchange held by a person resident in India upto such limit as the Reserve Bank may specify, if such foreign exchange was acquired by way of gift or inheritance from a person referred to in clause (*c*) including any income arising therefrom; (*e*) foreign exchange acquired from employment, business, trade, vocation, services, honorarium, gifts, inheritance or any other legitimate means upto such limit as the Reserve Bank may specify; and (*f*) such other receipts in foreign exchange as the Reserve Bank may specify.

Authorised Person

Chapter III of the Act relates to the authorisation of a person by the Reserve Bank to deal in foreign exchange, Reserve Bank's powers to issue directions to authorised person and the power of Reserve Bank to inspect authorised person. Section 10 of the Act says that the Reserve Bank may authorise any person to deal in foreign exchange or in foreign securities, as an authorised dealer, money changer or off-shore banking unit or in any other manner as it deems fit. The authorisation shall be in writing and shall be subject to the condition laid down therein. However, the Reserve Bank may revoke the authorisation (*a*) if it is in public interest to do so, or (*b*) if the authorised person has failed to comply with the condition subject to which the authorisation was granted or has contravened any of the provisions of the Act or any rule, regulation, notification, direction or order made thereunder. Section 11 empowers the Reserve Bank to give directions to the authorised person in regard to making of payment or the doing or desisting from doing any act relating to foreign exchange or foreign security to ensure compliance with the provisions of the Act. Section 12 empowers the Reserve Bank to inspect the business of any authorised person.

Contravention and Penalties

Chapter IV deals with the issue of contravention and penalties. Section 13 says that if any person contravenes any provisions of this Act, he shall, upon adjudication, be liable to a penalty upto thrice the sum involved in such contravention where such amount is quantifiable, or upto two lakh rupees where the amount is not quantifiable, and where such contravention is a continuing one, further penalty which may extend to five thousand rupees for every day after the first day during which the contravention continues. Section 14 says that if the person concerned fails to make full payment of the penalty imposed on him within a period of ninety days, he shall be liable to civil imprisonment. According to Sub-section 1 of Section 15, any contravention under Section 13 may, on an application made by the person committing such contravention, be compounded by the Director of Enforcement or such other officers as may be prescribed by the Central Government. Sub-section 2 of Section 15 says that where a contravention has been compounded under Sub-section 1, no proceeding or further proceeding, as the case may be, shall be initiated or continued as the case may be, against the person committing such contravention under that section, in respect of the contravention so compounded.

Adjudication and Appeal

Chapter V deals with the issue of adjudication and appeal. Section 16 states that the Central Government may appoint Adjudicating Authorities for holding an inquiry in the manner prescribed after giving the accused person a reasonable opportunity of being heard for the purpose of imposing any penalty. Section 17 provides for the appointment of one or more Special Directors (Appeals) to hear appeals against the orders of the Adjudicating Authorities. Section 18 says that the Central Government shall, by notification, establish an Appellate Tribunal to be known as the Appellate Tribunal for Foreign Exchange to hear appeals against the orders of the Adjudicating Authorities and the Special Director (Appeals) under this Act. The Appellate Tribunal shall consist of a chairperson and such number of Members as the Central Government may deem fit. Sub-section 2 of Section 28 which deals with the powers of the Appellate Tribunal and the Special Director (Appeals) states that they shall have, for the purposes of discharging their functions under this Act, the same powers as are vested in a civil court under the Code of Civil Procedure, 1908 while trying a suit. Section 35 lays down that any person aggrieved by any decision or order of the Appellate Tribunal may file an appeal to the High Court within sixty days from the date of communication of the decision or order of the Appellate Tribunal to him on any question of law arising out of such order.

Directorate of Enforcement

Chapter VI deals with the establishment of the Directorate of Enforcement and its powers, etc. Sub-section 1 of Section 36 states that the Central Government shall establish a Directorate of Enforcement with a Director and such other officers or class of officers as it thinks fit, who shall be called Officers of Enforcement, for the purpose of this Act. Sub-section 1 of Section 37 lays down that the Director of Enforcement and other officers of Enforcement not below the rank of an Assistant Director, shall take up for investigation the contravention referred to in Section 13. Sub-section 2 lays down that, without prejudice to the provisions of Sub-section 1, the Central Government may also, by notification, authorise any officer or class of officers in the Central Government, State Government or the Reserve Bank, not below the rank of an Under Secretary to the Government of India to investigate any contravention referred to in Section 13. According to Sub-section 3 of this section, the Director of Enforcement and other officers of Enforcement shall exercise the like powers

which are conferred on Income-tax authorities under the Income-tax Act, 1961 (43 of 1961) and shall exercise such powers, subject to such limitations laid down under that Act.

The Directorate of Enforcement is mainly concerned with the enforcement of the FEMA to prevent leakage of foreign exchange. The Directorate is also responsible for adjudication of cases and follow-up of complaints registered under the erstwhile FERA, 1973. This Directorate has also been entrusted with the implementation of Prevention of Money Laundering Act (PMLA), 2002, which has come with into force with effect from July 1, 2005. During the year 2005-06, the Directorate conducted 123 searches in which it seized Rs. 928 lakh in Indian currency and foreign currencies equivalent to Rs. 59 lakh. The Directorate recovered penalties of Rs. 995 lakh under FERA and Rs. 135 lakh under FEMA in 2005-06. The Directorate also confiscated substantial amounts of Indian currency and foreign currencies under FERA and FEMA. It adjudicated 475 FERA cases and 550 FEMA cases during 2005-06.[4]

Miscellaneous

The last chapter, chapter VII consisting of Sections 39 to 49 deals with miscellaneous issues. Sub-section 1 of Section 40 empowers the Central Government in the public interest and by notification to suspend or relax the provisions of the Act in certain circumstances. Section 42 provides that where contravention of any of the provisions of this Act is committed by a company, the person responsible for the conduct of its business shall be deemed to be guilty of the contravention. Section 46 empowers the Central Government to frame the rules and Section 47 empowers the Reserve Bank to make regulations to carry out the provisions of this Act and the rules made thereunder. Section 49 provides for repeal of the Foreign Exchange Regulation Act, 1973 and for dissolution of the Appellate Board constituted under Section 52 of the said Act.

FEMA : A MAJOR DEPARTURE FROM FERA

As is clear from the name of the Act itself, the ***emphasis under FEMA is on 'exchange management' whereas under FERA the emphasis was on 'exchange regulation' or exchange control.*** Under FERA it was necessary to obtain Reserve Bank's permission, either special or general, in respect of most of the regulations thereunder. FEMA has brought about a sea change in this regard and except for Section 3, which relates to dealing in foreign exchange, etc., no other provisions of FEMA stipulate obtaining Reserve Bank's permission.[5] The demand for new legislation was basically on the following counts: (*i*) FERA was introduced in 1974 when India's foreign exchange reserve position was not satisfactory. Accordingly, stringent controls were required on the use of foreign exchange. With improvement in foreign exchange position, it is argued that such stringent controls are not now required; (*ii*) India had given notice to the IMF in August 1994 that it had attained Article VIII status. This notice meant that no restrictions will be imposed on remittances of foreign exchange on account of current account transactions; and (*iii*) the private corporate sector had been complaining for long against, what it termed, the 'draconian provisions' of FERA which gave unbridled powers to the Enforcement Directorate to arrest any person, search any premises, seize documents and start proceedings against any person for contravention of FERA or for preparations to contravention of FERA. The contravention under FERA was treated as a criminal offence and the burden of proof was on the guilty.[6]

FEMA has changed all this. As stated earlier, the purpose of FEMA is to 'facilitate external trade and payments' and 'promote the orderly development and maintenance of foreign exchange market in India.' As far as the promotion of orderly development and maintenance of foreign exchange market is concerned, FEMA is silent. However, as far as facilitating external trade is concerned, Section 5 of the Act removes restrictions on drawal of foreign exchange for the purpose of current account transactions. As external trade, i.e. import and export of goods and services, involves transactions on current account, there will be no need for seeking the permission of Reserve Bank of India in connection with remittances involving external trade. However, Section 5 confers power on the Central Government to impose reasonable restrictions on current account transactions, in consultation with the Reserve Bank. But this seems to be just an 'enabling provision' added keeping in view the experiences of some East-Asian countries during the 1997-98 crisis which required stricter exchange controls.[7] As far as the 'draconian provisions' are concerned, FEMA has reduced their rigour significantly. For instance, unlike in the case of FERA, violations of FEMA will not attract criminal proceedings. The contravention will now be treated as a civil offence. Thus FEMA removes the "threat of imprisonment" which businessmen abhor. Now they will either compound their illegal acts by paying a fine if it is not too high, otherwise they will pay lawyers to engage in lengthy (and mostly inconclusive) litigation with the government.

According to Biswajit Dhar and Mritunjoy Mohanty, FEMA represents major departures from the past policies in two important respects: "First, it can be seen as an initial step towards capital account convertibility. Secondly, by removing the FERA from the statute book and replacing it with the FEMA, the government seems to have finally decided to give up even the bare intention of regulating foreign capital in the country."[8] The latter is an important message coming at a time when the international institutions, under the leadership of developed countries, are putting a multilateral investment regime in place that would free foreign investors from any controls which host countries might feel the need to impose. Although India has maintained that it would preserve its sovereign rights to regulate foreign investment, the absence of FERA is likely to pose serious difficulties in this effort.

As far as the issue of capital account convertibility is concerned, Section 6 of FEMA introduces some elements in this respect. As mentioned earlier, Sub-section 2 of this Section states that "... Reserve Bank shall not impose any restriction on the drawal of foreign exchange for payments due on account of amortization of loans or for depreciation of direct investments in the ordinary course of business". This leaves out an important set of capital account transactions outside the Reserve Bank's ambit. In this context, there are two points worth noting: "First, as the above quote makes clear, international investors have been assured that their interests will be protected : a matter of no small importance given the current state of multilateral negotiations aimed at deregulating foreign investment. Second, in a world where loans are fungible, the above could well be the thin end of the wedge which expands the scope of convertibility."[9]

NOTES

1. This objective originally read as 'to regulate the import and export of currency and bullion' but the words 'and bullion' were omitted by the Foreign Exchange Regulation (Amendment) Act, 1993 with effect from January 8, 1993.
2. For a discussion of some of these concessions see the section on 'Indian Government's Policy Towards Foreign Capital' in Chapter 43 on 'Foreign Investment, Technology and Multinational Corporations.'
3. *Foreign Exchange Management Bill 1998 & Prevention of Money-Laundering Bill 1998* (Taxmann, 1998), p. 18.
4. Government of India, *India 2007- A Reference Annual* (New Delhi, 2007), pp. 402-3.
5. Rashmin Sanghvi, Naresh Ajwani and K.C. Chaudhari, *Guide to Foreign Exchange Managment Act, 1999* (New Delhi: Taxmann Allied Services Private Ltd., 1999), p. 12.
6. *Ibid.*, p. 14.
7. *Ibid.*, p. 13.
8. Biswajit Dhar and Mritunjoy Mohanty, "FEMA : A Closer Look", *Economic and Political Weekly,* October 3, 1998, p. 2569.
9. *Ibid.*, p. 2569.

CHAPTER

30 CONSUMER PROTECTION

The Need for Consumer Protection
Steps Required for Consumer Protection
Consumer Protection: How ?
• Imposition of Self Regulation and Discipline • Voluntary Organisations of Consumers • Spreading Information and Awareness • Government Legislation • Other Steps
Consumer Protection Act, 1986 (With Amendments)
• Objectives of the Act and Rights of Consumers • Consumer Protection Councils • Consumer Disputes • Redressal Agencies • Remedial Action • Implementation of the Act

In this chapter devoted to a discussion of consumer protection, we aim to address the following questions :

- What is the need for consumer protection and what steps are required to protect the interest of consumers ?
- What are the various methods of consumer protection ?
- What are the main provisions of Consumer Protection Act, 1986 ?

THE NEED FOR CONSUMER PROTECTION

In India consumers spread over the entire length and breadth of the country are unorganized. Many of them are also illiterate, poor and backward. As against this, the producers are relatively much more organised. They have huge resources at their disposal and can deceive and exploit consumers in a number of ways. In a bid to beat competition, increase their market share and maximise their profits, they, at times, adopt dubious means to push up the sales of their products.

What are the ways in which producers and traders can deceive consumers ? The following are the most popular :

1. Prices may be fixed at levels much higher than those dictated by the costs of production.
2. The sellers may first hike prices and then offer discounts to attract consumers.
3. The consumers may not be given the correct weight or quantity of goods.
4. Advertisement might make false claims about the quality of the goods.
5. Advertisement may provide incomplete information not disclosing the risks associated with the use of the products.
6. The goods supplied to the consumers may be highly adulterated.

Prices in India have been increasing by leaps and bounds over the last three-four decades. Naturally they have affected the consumers, particularly those belonging to the poor classes or the lower middle income groups very adversely. A number of causes are responsible for pushing up the prices and it is not possible to single out any particular cause. However, it has been observed that in a number of cases the producers intentionally restrict output to raise prices by forming cartels amongst themselves and adopting restrictive trade

practices. In some cases the price that a consumer is asked to pay has no relation to the cost of production. This often happens in the case of drugs whose prices are generally kept much higher than their cost of production. Another practice that is becoming increasingly popular to deceive consumers is the offer of heavy discounts on prices. The traders often raise the prices arbitrarily and then offer discounts. As a result, the unsuspecting consumer may actually be shelling out even a higher price than the actual price of the product.

Often advertising is another means used by producers to deceive consumers. The actual purpose of advertising is informing the consumer about different products. To this extent, it is useful. However, it has a number of ill effects, the two most important being the following : (*i*) the cost of advertising is added to the selling cost and this increases the prices; and (*ii*) it can be deceptive and can misguide the consumers. Companies can claim qualities with no scientific basis and they can keep the consumers in dark by not disclosing the risks associated with the use of their products. Worldwise, advertising is now a $ 435 billion business. But that's a conservative estimate of annual global expenditures. If all forms of marketing are included, the figure rises to nearer $ 1 trillion. In fact, global advertising has increased by seven times since 1950, growing a third faster than the world economy. The growth in advertising expenditure has been particularly rapid in the countries of Asia and Latin America especially since the mid-1980s and the early 1990s. Over the past 10 years individual countries in this region have shown spectacular advertising growth—for China more than 1,000 per cent, for Indonesia 600 per cent, for Malaysia and Thailand more than 300 per cent, and for India, the Republic of Korea and the Phillippines more than 200 per cent. Compared with GDP levels, the advertising expenditures in developing countries are particularly high.[1]

The worst hazard that has appeared in India in recent times is the widespread practice of adulteration. Adulteration is practised by private trade at several points in the supply chain—right from the producer to the ultimate consumer. In agricultural commodities adulteration is widespread. Small pebbles are mixed in wheat, jowar, bajra and maize. Leaves and bark of some trees are mixed with tea and sold as tea. Butter is mixed with coloured vanaspati, chilli powder with dust, spices with sand, yellow mud, saw dust etc. Adulteration in milk is also quite common. The worst criminals are the manufacturers and dealers of spurious drugs as they play havoc with the lives of people.

STEPS REQUIRED FOR CONSUMER PROTECTION

On account of the above factors, a strong public opinion has built up over the years demanding protection to consumers. Protection to consumers requires the recognition of the following rights of the consumers by the business and the government:

1. The right to safety. Consumers should have right to protection of health and life against goods which are hazardous to health and life.

2. The right to be informed. Consumers should be given proper information about the goods that they intend purchasing. They should be protected against wrong and misleading advertisement.

3. The right to choose. Consumers should be given the right to choose from a variety of goods. This will give them an opportunity to select goods of their choice. In addition, because of competition, the prices charged would be reasonable.

4. The right to be heard. Consumers should be given a 'sympathetic ear' by the government. Their complaints and grievances should be properly looked into.

5. The right to get redress. It is not enough to hear the complaints of the consumers. It is also necessary to take action on these complaints as early as possible. For this purpose an appropriate redressel machinery must be in place.

According to *Human Development Report,* 1998, consumer rights must be defended through (*i*) Strict standards for consumer health and safety: (*ii*) Product labelling about the content and proper use of products and their environmental and social impact; (*iii*) Information and awareness campaigns about potential health hazard, such as smoking and the improper use of feeding formula for infants.[2]

CONSUMER PROTECTION : HOW ?

The most important methods for consumer protection are as follows:

1. Imposition of self-regulation and discipline on themselves by the manufacturing and trading community.
2. Voluntary organisation of consumers to safeguard their interests.

3. Spreading information and awareness regarding different products.
4. Government legislation to stop the malpractices resorted to by the traders and manufacturers.

Imposition of Self Regulation and Discipline

The imposition of self regulation and discipline by the manufacturers and traders on themselves is a *very desirable* but *least feasible* method of consumer protection. Only a handful of producers and traders will agree to impose self-discipline on themselves. Most others will not participate in this self-regulation at all while many will only support it verbally without doing anything concrete. The fact is that there are many unscrupulous traders operating with the sole intention of earning profits without caring for the means they adopt to achieve this purpose. How can they be expected to agree to self-regulation ? A new approach that has been adopted with considerable success in this regard in recent years is 'publicizing' certain vital information and then requiring businesses to report their 'level' of adherence to this information. For instance, in some countries, the governments publicize information on industrial polluters. This encourages the production of information about pollution generation, both as a source of incentive for behavioural change and as a benchmark for subsequent regulation. A well known example is the US Toxic Release Inventory, which requires businesses to report the amounts of toxic materials that they put into the environment. Many companies respond by reducing pollution to preserve their reputation.[3]

Voluntary Organisations of Consumers

In many countries, developed as well as developing, consumers have organised themselves on a voluntary basis. The organisation is often achieved by (*i*) setting up consumer associations or councils, or (*ii*) organising consumer cooperatives.

Consumer Associations or Councils. Consumer associations or Consumer councils have been formed in most of the developed countries and some developing countries with an eye on protecting the rights of consumers. In India, a nucleus consumer organisation named National Consumer Service (NCS) was set up in 1963. Its main object was to collect market intelligence, publish bulletins for information of consumers, study the trends of rising prices, and organise activities against the malpractices of the trade. Some councils and consumer associations affiliated to NCS were set up in Delhi. Another consumer organisation named Price Rise Resistance Movement (PRRM) was set up in Delhi in 1964. It organised meetings to protect against rising prices. Open air shops were also formed for the sale of vegetables, fruits, eggs, etc. In 1966 a Consumer Guidance society was set up in Mumbai. It was a voluntary organisation set up to promote and protect the rights and interests of consumers. It provides information and guidance to consumers, campaigns against adulteration of goods by traders and publishes test results of consumer goods. A consumer organisation 'Common Cause' set up by H.D. Shourie and based at Delhi, is also doing yeoman's service in the field of educating consumers and protecting their rights. A National Consumer Council of India was formed in Delhi in 1968.

Consumer Cooperatives. A consumer cooperative is a voluntary association of individuals formed for the achievement of the common good. In India, any ten or more persons belonging to a particular place, class or occupation can come together to form a cooperative society. They can apply to the Registrar of Cooperative Societies for registration. Some of the advantages of consumer cooperatives are as follows: (1) Since a number of individuals come together to form a consumer cooperative, their bargaining power increases. (2) Since purchases are made in bulk, the are generally at lower prices. (3) Consumers are assured of unadulterated and standard quality goods. (4) Correct weights and measures are used by the society therefore the consumer is saved from 'deceit' on this account also. (5) Goods are sold at market prices to avoid unhealthy competition with other retailers. The profits earned on this account are usually spent on various social programmes for the benefit of members. (6) In our country consumer cooperatives have performed the function of distributing essential commodities at reasonable prices.

As a policy, Government of India have been emphasizing the need for strengthening cooperatives, so as to enable these organisations to play a dominant role in the Public Distribution System both in the urban and in the rural areas. The consumer corporative structure in the country has four tiers, with the National Cooperative Consumers Federation of India Limited (NCCF) at the national level. Thirty State Cooperative Consumers Organisations are affiliated to the NCCF. At the central/wholesale level, there are 800 consumer cooperative stores. At the primary level, there are 21,903 primary stores. In the rural areas, there are about 44,418 village level Primary Agricultural Credit Societies and Marketing Societies undertaking the distribution of consumer goods alongwith their normal business. In the urban and semi-urban areas the consumer cooperative societies are operating about 37,226 retail outlets to meet the requirements of the consumers. The NCCF besides

undertaking distribution of consumer articles, also has a consultancy and promotional cell for strengthening consumer cooperative societies engaged in the retaailing activities. NCCF with its Head Office at New Delhi has 34 branches/sub-branches located in various parts of the country. The government with the help of NCCF, launched a scheme called *Sarvpriya* in July 2000. The scheme envisages distribution of 11 selected commodities of daily use to the consumers through the fair price shops and consumer cooperatives. The sales turnover of NCCF during 2005-06 was Rs. 630 crore[4].

Spreading Information and Awareness

Globalisation—the integration of trade, investment and financial markets—has also integrated the consumer market. Globalisation is bringing a constant stream of new products, produced far away in unknown conditions. In such circumstances, information and awareness regarding different products becomes essential. Unfortunately, the predominant source of product information available today in most of the countries across the globe is commercial advertising. If unchecked, commercial advertising can be deceptive as its main objective is to 'lure' consumers to use a certain product and not to inform or educate them regarding the risks or hazards associated with the use of that product. Thus, while marketing and advertising campaigns have intensified, information campaigns lag far behind (particularly in the developing countries). This is due to the fact that while massive expenditures are being incurred on commercial advertisements, resources for information campaigns are always seriously limited.

Government Legislation

Governments of most of the countries have adopted various legislations for the protection of consumer rights. For example, the British and US governments have enacted a number of laws which have served as a guide for other countries. The important British laws in this respect are: (*i*) The Sale of Goods Act, 1893, (*ii*) The Food and Drugs Act, 1955, (*iii*) The Weights and Measures Act, 1963, (*iv*) The Trading Stamps Act, 1964, (*v*) The Fair Trading Act, 1973 etc.

The Government of India have also passed a number of Acts to protect the rights of consumers. These include Agricultural Produce (Grading and Marketing) Act, 1937; the Essential Commodities Act, 1955; the Weights and Measures Act, 1958; Prevention of Food Adulteration Act, 1954; the Drugs and Cosmetics Act, 1940; Fruit Products Order 1955; the Prevention of Black Marketing and Maintenance of Supplies of Essential Commodities Act; the Drugs and Magic Remedies (Objectionable Advertisements) Act; the Dangerous Drugs Act; the Indian Standards Institution (Certification Mark) Act; the Indian Sale of Goods Act; the Indian Contract Act; the Emblems and Names (Preventing of Improper Use) Act; Packaged Commodities (Regulation) Order, 1975; the Trade and Merchandise Mark Act; Monopolies and Restrictive Trade Practices Act, 1969 etc. The most important legislation in the field of consumer protection is the Consumer Protection Act, 1986, to which we turn in the next section.

Other Steps

Under 'other steps' we shall consider (*i*) Conferment of National Awards, (*ii*) Publicity measures, (*iii*) Consumer Welfare Fund, and (*iv*) Bureau of Indian Standards.

National Awards. To encourage the participation of consumer organisations, women and youth in the field of consumer protection, the Ministry of Civil Supplies, Consumer Affairs and Public Distribution of the Government of India has instituted three National Awards namely National Award on Consumer Protection, National Women Award and National Youth Award on Consumer Protection which are given every year.

Publicity Measures. The fifteenth of March is celebrated as "World Consumer Rights Day" all over the world. This day is used to spread consumer awareness through various means like display of hoardings, banners, bus panels etc. In India, Doordarshan and AIR also regularly broadcast programmes on consumer protection and brochures and booklets (like 'Salient Features of Consumer Protection Act, 1986', 'Rights of Consumers', 'The Consumer Protection Act and You', 'Help Prevent Adulteration', 'Consumer Protection and Weights and Measures', 'Directory of Consumer Organisations' etc.) are published. In addition, 24 December has been declared as 'National Consumer Day'.

Consumer Welfare Fund. The Government of India created the Consumer Welfare Fund (CWF) in 1992 with the objective to provide financial assistance to protect and promote the welfare of the consumers, develop consumer awareness and strengthen the consumer movement in the country particularly in the rural areas. The Fund, set up by the Department of Revenue under the Central Excise and Salt Act, 1994, is operated by the Ministry of Consumer Affairs, Food and Public Distribution.

Schemes under CWF included : (*i*) Jagriti Shivir Yojana (launched in June 2001); (*ii*) setting up of District Consumer Information Centre in a phased manner; (*iii*) setting up of consumer clubs in schools and colleges; and (*iv*) promoting involvement of research institutions/universities/colleges etc. in consumer protection and welfare. With the closure of funding of Jagriti Shivir Yojana and District Consumer Information Centre by the Department of Consumer Affairs, the State Governments are now being impressed upon to create their own Consumer Welfare Fund.

Bureau of Indian Standards. The Bureau of Indian Standards (BIS) is the national standards body of India. The main functions of BIS include preparation and implementation of standards, operation of certification schemes—both for products and quality system, organisation and management of testing laboratories, consumer awareness and maintaining close liaison with international standards bodies. As on March 31,2006, 18,219 Indian Standards are in force covering important segments of the economy which serve the industry in upgrading the quality of their goods and services.

BIS Product Certification Marks Scheme provides the consumer an assurance of quality conformance to national standards. The total number of operative licences have risen to 19,558 as on March 31, 2006, covering 1,198 different items ranging form food products to electronics. The scheme is basically voluntary in nature. However, keeping in view the safety and mass consumption of certain products, it has been made mandatory for 110 items like LPG cylinders, food colours, packaged drinking water etc.

CONSUMER PROTECTION ACT, 1986 (WITH AMENDMENTS)

Objectives of the Act and Rights of Consumers

Enactment of Consumer Protection Act, 1986 was one of the most important steps taken to protect the interest of the consumers. It was formulated after studying intensively the consumer protection Acts of a number of countries, and after thorough consultations with the representatives of consumers, traders and industrialists. All the provisions of the Act came into force with effect from July 1, 1987. The Act was thoroughly amended in 1991 and 1993. To make the Consumer Protection Act more functional and purposeful, a comprehensive amendement was carried out in December 2002 and brought into force from March 15, 2003. As a sequel, the Consumer Protection Rules, 1987 were also amended and Consumer Protection Regulations, 2005 framed to give effect to the provisions of the Act.

The objective of the Consumer Protection Act is ***"to provide for the better protection of the interest of consumers and for that purpose to make provision for the establishment of consumer councils and other authorities for the settlement of consumers' disputes and for matters connected therewith."*** The Act applies to all goods and services especially exempted by the Central Government. It covers all the sectors whether private, public or co-operative. The provisions of the Act are compensatory in nature.

Section 6 (Chapter II) of the Act enshrines the following rights of consumers:

(*a*) the right to be protected against the marketing of goods and services which are hazardous to life and property;

(*b*) the right to be informed about the quality, quantity, potency, purity, standard and price of goods or services so as to protect the consumer against unfair trade practices;

(*c*) the right to be assured, wherever possible, access to a variety of goods and services at competitive prices;

(*d*) the right to be heard and to be assured that consumers' interests will receive due consideration at the appropriate fora;

(*e*) the right to seek redressal against unfair trade practices or unscrupulous exploitation of consumers; and

(*f*) the right to consumer education.

Consumer Protection Councils

The Act provides for the establishment of a Central Consumer Protection Council by the Central Government and State Consumer Protection Councils by the respective State governments. The Central Council shall consist of the following members, namely (*a*) the Minister incharge of consumer affairs in the Central Government, who shall be the chairman, and (*b*) such number of other official or non-official members representing such interests as may be prescribed. The Central Council shall meet as and when necessary, but at least one meeting

of council shall be held every year. The objects of the Central Council are to promote and protect the rights of consumers noted above (clauses (*a*) to (*f*) of Section 6.)

The State Council shall be established by the State Government in question and shall consist of the following members: (*a*) the Minister incharge of consumer affairs in the State Government who shall be the chairman, and (*b*) such number of other official or non-official members representing such interests as may be prescribed by the State government. The State Council shall meet as and when necessary but not less than two meetings shall be held every year. The objects of every State Council shall be to promote and protect within the State rights of the consumers laid down in clauses (*a*) to (*f*) of Section 6.

Consumer Disputes Redressal Agencies

Section 9 of the Consumer Protection Act provides for the establishment of a three-tier consumer disputes redressal system at the District, State and National level. The three redressal agencies are as follows:

1. A Consumer Disputes Redressal Forum at the District level known as the 'District Forum.'
2. A Consumer Disputes Redressal Commission at the State level known as the 'State Commission.'
3. A National Consumer Disputes Redressal Commission established by the Central Government.

Section 10 of the Act is concerned with the composition of the District Forum, Section 16 with the composition of the State Commission and Section 20 with the composition of the National Commission.

Section 11 relates to the jurisdiction of the District Forum. According to this Section, subject to the other provisions of this Act, the District Forum shall have jurisdiction to entertain complaints where the value of the goods or services and the compensation, if any, claimed does not exceed rupees twenty lakhs. According to Section 12, a complaint in relation to any goods or services sold may be filed with a District Forum by: (*i*) the consumer to whom such goods or services are sold; (*ii*) any recognised consumer association (whether the consumer in question is a member of that association or not); (*iii*) one or more consumers, where there are numerous consumers having the same interest; or (*iv*) the central government or the State government either in its individual capacity or as a representative of the interests of consumers in general.

Section 17 relates to the jurisdiction of the State Commission. According to this Section, subject to the other provisions of the Act, the State Commission shall have jurisdiction to entertain complaints where the value of the goods or services and the compensation, if any, claimed exceeds Rs. 20 lakh but not Rs. 1 crore. Section 21 relates to the jurisdiction of the National Commission. According to this Section, subject to other provisions of the Act, the National Commission shall have jurisdiction to entertain complaints where the value of goods or services and the compensation, if any, claimed exceeds Rs. 1 crore.

Remedial Action

If any of the consumer redressal agencies is satisfied that the goods complained against suffer from any of the defects specified in the complaint or that any of the allegations contained in the complaint about the services are proved, it shall issue an order to the opposite party to do one or more of the following things namely—

(*a*) to remove the defect pointed out by the appropriate laboratory from the goods in question;
(*b*) to replace the goods with new goods of similar description which shall be free from any defects;
(*c*) to return to the complainant the price or, as the case may be, the charges paid by the complainant;
(*d*) to pay such amount as may be awarded by it as compensation to the consumer for any loss or injury suffered by the consumer, due to the negligence of the opposite party;
(*e*) to remove the defects in goods or deficiencies in the services in question;
(*f*) to discontinue the unfair trade practice or the restrictive trade practice or not to repeat them;
(*g*) not to offer the hazardous goods for sale;
(*h*) to withdraw the hazardous goods from being offered for sale;
(*i*) to provide for adequate costs to parties.

Appeal. According to Section 15, any person aggrieved by an order made by the District Forum may prefer an appeal against such order to the State Commission within a period of 30 days from the date of the order, in such form and manner as may be prescribed. Any person aggrieved by an order of the State Commission may prefer an appeal against such order to the National Commission within a period of 30 days (Section 19). In case a person is aggrieved by the order made by the National Commission, he may prefer an appeal against such order to the Supreme Court within a period of 30 days from the date of the order (Section 23). (In all cases, the appeal can be entertained even after the expiry of 30 days provided that the authority (redressal

agency) to whom such appeal is being made is satisfied that there was sufficient cause for not filing it within that period.)

Penalties. Section 27 pertains to the issue of penalties. According to this Section, where a trader or a person against whom a complaint is made or the complainant fails or omits to comply with any order made by the redressal agency, he shall be punishable with imprisonment for a term which shall not be less than one month but which may extend to three years, or with fine which shall not be less than Rs. 2,000 but may extend to Rs. 10,000 or with both.

Dismissal of Frivolous or Vexatious Complaints. Where a complaint instituted before any redressal agency is found to be frivolous or vexatious, the redressal agency shall dismiss the complaint and make an order that the complainant shall pay to the opposite party such cost, not exceeding Rs.10,000 as may be specified in order.

Implementation of the Act

In terms of the Consumer Protection Act, Consumer Disputes Redressal Agencies have been set up at the district level (600), State level (35) and National level to provide simple, inexpensive and time bound justice to the consumer complaints against defective goods, deficient services including the unfair/trade practices adopted by the traders or any person. States have been empowered to establish additional District Fora in the same District. States can also establish additional benches of the State Commissions and also notify places to hold circuit benches. The Central government set up the National Commission in 1988 at New Delhi. The Act empowers appointment of additional members of the National Commission for creation of additional benches as also for heading of circuit benches by the National Commission to bring justice to the doorstep of the consumers. At present, 3 benches are functioning in the National Commission.

Since the inception of the three tier redressal agencies upto the period April 2006, 41,832 cases were filed in the National Commission out of which 34,231 cases have been disposed of, 3,71,375 cases were filed in the State Commissions out of which 2,62,704 cases have been disposed of, and 21,75,550 cases were filed in the District Fora out of which 19,50,209 cases have been disposed of. Altogether 25,88,757 cases were filed in the three-tier redresal agencies out of which 19,50,209 cases have been disposed of which is remarkable as it gives a disposal rate of 87 per cent.[5]

The Government of India also created a separate Department of Consumer Affairs in the year 1997 to act as the nodal department to exclusively focus on protecting the rights of consumers including redressal of consumer grievances as well as to promote standards of goods and services etc. On the request of the Central government, some State governments have created separate Departments/Directorates of Consumer Affairs and, wherever it has not been feasible to do this, at least the names of the Departments have been changed to include Consumer Affairs/Consumer Protection for the knowledge of the general public. The Central government has recently requested all the States/Union Territories to establish a separate Department with full fledged Secretary so that the consumer protection programme gets exclusive attention for protecting and promoting the welfare of consumers.

NOTES

1. United Nations Development Programme, *Human Development Report 1998*, p. 63.
2. *Ibid.*, p. 11.
3. *Ibid.*, p. 11.
4. Government of India, *India 2007- A Reference Annual* (New Delhi, 2007), p. 432.
5. *Ibid.*, p. 434-5.

UNIT 6

Indian Industrial and Trade Environment

31. Industrial Growth and Diversification
32. Industries (Development and Regulation) Act, 1951 and Industrial Licensing
33. Public Sector in the Indian Economy
34. Private Sector in the Indian Economy
35. Privatisation and Disinvestment
36. Modern Corporations and the Company Law
37. Mergers and Acquisitions
38. MRTP Act, 1969 and Competition Act, 2002
39. Small-Scale and Cottage Industries
40. Industrial Sickness in India
41. Trends in Foreign Trade and Structural Changes
42. India's Balance of Payments
43. Foreign Investment, Technology and Multinational Corporations

If Indian industry is to be placed on the path of recovery a combination of some degree of protection against the displacement by imports and a faster pace of expansion of the home market is an absolute necessity. Thus, in the short run, some protection and greater fiscal stimulus (financed with larger direct tax revenues) appear to be the only available sources of growth. In the medium term and long run, however, the government would have to devise ways of expanding the market for mass consumption goods. This requires a programme to place purchasing power among that section of the Indian population that remains abysmally poor despite 50 years of independent development.

— C.P. Chandrasekhar

CHAPTER

31 INDUSTRIAL GROWTH AND DIVERSIFICATION

Programmes for Industrial Development Under the Plans
Trends in Industrial Production
• Phase I (1951-1965): Building up of Strong Industrial Base • Phase II (1965-80): Industrial Deceleration and Structural Retrogression • Phase III (1981-1991): The Period of Industrial Recovery • Phase IV (The Period 1991-92 Onwards)
Industrial Diversification— Changes in Industrial Structure During the Planning Period
• Changes in Industrial Structure in 1990s

At the time of Independence, India was industrially and economically backward. Even in 1951-52 (the year when First Five Year Plan was initiated), the primary sector (agriculture, forestry and logging, fishing, mining and quarrying) accounted for 58.9 per cent of GDP at factor cost whereas the secondary sector (manufacturing, construction, electricity, gas and water supply) accounted for just 13.6 per cent of GDP at factor cost (at 1993-94 prices). The strategy of long-term development spelt out in the Second Five Year Plan gave high priority to programmes of industrialization. This was on account of a number of reasons. ***First***, the country was industrially backward, and as such, the establishment of new industries on a big scale and development of the traditional industries was an imperative necessity. ***Secondly***, productivity of labour is the highest in manufacturing industries. Therefore, for raising national income at a fast rate there is no way out except to establish industries. ***Thirdly*** the pressure of population on land is excessive and unless surplus workforce is transferred to other sectors, agriculture's potential cannot be fully realised. Hence, development of the industrial sector is a pre-condition for agricultural development. ***Finally***, industrialization induces development in other sectors. For example, when industries create demand for the agricultural products, such as cotton, jute, oilseeds and sugarcane, their output is raised by the farmers. Further, with the development of industries, supply of fertilizers, insecticides, farm implements etc. increases, which helps in raising agricultural productivity. Development of transport, communications and energy is still more dependent on industrial growth.

In this chapter we propose to discuss the programmes for industrial development in India and address the following questions:

- What have been the trends in industrial growth during the pre-reform (*i.e.* pre-1991) period and post-reform (i.e. post-1991) period ?
- What have been the causes of unsatisfactory performance of the industrial sector in the post-reform period ?
- What changes have taken place in the industrial structure during the period of planning ? How has the policy of liberalisation being pursued by the Government of India since 1991 influenced the industrial sector ?
- What are the problems being faced by the industrial sector ?

PROGRAMMES FOR INDUSTRIAL DEVELOPMENT UNDER THE PLANS

Because of the emphasis laid on programmes of industrialisation during the planning period, the allocations to the industrial sector increased considerably. For example, ***while the First Plan spent only Rs. 55 crore out of a total expenditure of Rs. 1,960 crore (i.e. a mere 2.8 per cent) on industry and minerals,[1] this expenditure was hiked to Rs. 938 crore under the Second Plan (which was 20.1 per cent of the total expenditure of Rs. 4,672 crore under the Plan) and further to Rs. 1,726 crore in the Third Plan (which was 20.1 per cent of the total expenditure of Rs. 8,577 crore under the Plan).*** Moreover, specific attention was paid to the establishment of basic and capital goods industries on a large scale so that a strong base for industrial development in the future could be built. This strategy (based on Mahalanobis Model) was spelt out in the Second Plan in the following words: "If industrialization is to be rapid enough, the country must aim at developing basic industries and industries which make machines to make the machines needed for further development. This calls for substantial expansion in iron and steel, non-ferrous metals, coal, cement, heavy chemicals and other industries of basic importance..." Third Five Year Plan also pressed forward with the establishment of basic capital and producer goods industries — with special emphasis on machine building programme — so that the growth of the economy in the subsequent plans could become self sustaining. As a result, programmes for expansion and diversification of capacity of the heavy engineering and machine building industries, castings and forgings, alloys tool and special steels, iron and steel and ferro-alloys, and steps to increase the output of fertilisers and petroleum products were undertaken. Efforts were also made to increase the production of major basic raw materials and producer goods like aluminium, mineral oils, dissolving pulp, basic organic and inorganic chemicals and intermediates inclusive of products of petro-chemical origin.

The above discussion shows that the Second and Third Plans placed great emphasis on building up the capital goods industries and basic industries. As a result, the industrial structure built up over these plans was heavily biased in favour of these industries. Most of these industries were set up in the public sector with the result that the size of the public sector also grew rapidly. The growth of the consumer goods industries was mostly left to the private sector. This structure of industrial development was promoted and nurtured in the Fourth and Fifth Plans also with minor changes here and there. ***Out of the total expenditure of Rs. 15,779 crore in the Fourth Plan, industry received Rs. 2,864 crore (i.e. 18.2 per cent of the total). The expenditure on industry was hiked to 22.8 per cent (Rs. 8,989 crore out of the total of Rs. 39,426 crore) in the Fifth Plan.***

In a review of industrial development over the thirty years of planning, the Sixth Plan noted that industrial production had increased by about 5 times during this period. More important than this quantitative increase in output was the fact that the industrial structure had been widely diversified covering broadly the entire range of consumer, intermediate and capital goods. However, noted the Plan, the structure of industrial development was not sufficiently guided by cost considerations. Thus industries tended to get established at sub-optimal capacities, leading to a high cost industrial structure. The Plan also noted that the public sector had failed to generate enough resources and that the problem of regional disparities in industrial development was as serious as ever. In fact, new industries had tended to gravitate towards existing centres and the backward areas had remained substantially untouched by planning.

In the light of the above, the Sixth Plan emphasised optimum utilisation of existing capacities and improvement of productivity, enhancement of manufacturing capacity, special attention to the capital goods industry and electronics industry, improvement in energy efficiency, dispersal of industry etc. ***Of the total expenditure of Rs. 1,09,292 crore under the Sixth Plan, the share of the industrial sector was Rs. 15,002 crore which comes to 13.7 per cent.*** The period of the Sixth Plan saw wide range changes in the industrial policy of the government. The industrial and trade policies were substantially liberalised. As a result, industrial production started picking up but it also created certain distortions in the economy as the import intensive sector of consumer durables and the group of chemicals, petro-chemicals and allied industries marched much ahead of other sectors and groups of industries.

The overall outlay envisaged in the Seventh Plan for industrial and mineral programmes (as stated earlier, data on village and small-scale industries are excluded) in the public sector was Rs. 19,663 crore. As against this, ***the actual expenditure was Rs. 25,971 crore which is 11.9 per cent of the total expenditure of Rs. 2,18,730 crore in the Seventh Plan.*** Industrial production was targeted to grow at the rate of 8.7 per cent per annum. The actual average rate of growth during the Seventh Plan works out at 8.5 per cent per annum. As far as the Eighth Plan is concerned, the overall outlay for industrial and mineral programmes in the public sector was kept at Rs. 40,588 crore. This was only 9.3 per cent of the total outlay of Rs. 4,34,100 crore in the plan.

This reduced allocation to industry and minerals in the Eighth Plan is in line with the liberalisation measures announced in the New Industrial Policy of 1991, according to which, the private sector is now destined to play an increasingly important role in industrial activities, especially in those fields where security and strategic or social considerations are not important. The public sector is expected to concentrate increasingly on basic and core sectors. Data on actual expenditure on the industrial sector in the Eighth Plan reveal that ***the actual expenditure on industry during the Eighth Plan period was just Rs. 40,623 crore out of the total Plan expenditure of Rs. 4,85,457 crore. This comes to just 8.4 per cent of total expenditure under the Eighth Plan.***[2]

In line with the liberalisation of industrial policy, the Eighth Plan also placed less emphasis on quantitative targets. It sought to achieve the desired growth in different sectors primarily through modifications in industrial, trade, fiscal policies and changes in duties and taxes rather than through quantitative restriction on imports/exports or licensing mechanism. The Plan envisaged a growth of 7.3 per cent per annum in the manufacturing sector. This target was achieved as the actual rate of growth turned out to be 7.4 per cent per annum.

The Ninth Plan outlay for industry and minerals was kept at Rs. 65,148 crore (the Ninth Plan allocations were made broad sector-wise therefore this includes data on village and small-scale industries as well). This was 7.6 per cent of the total Plan outlay of Rs. 8,59,200 crore. However, ***the actual expenditure on industry and minerals in the Ninth Plan was only Rs. 40,408 crore which was just 5.0 per cent of total actual expenditure in the Plan.***[3] ***The Ninth Plan envisaged an industrial growth rate of 8.2 per cent per annum while the actual*** growth rate was only 5.0 per cent.

The Tenth Five Year Plan proposed an outlay of Rs. 58,939 crore for industry and minerals which was just 3.9 per cent of the total outlay of Rs. 15,25,639 crore. The reduced allocation to industry is in line with the government's strategy to liberalise and privatise and give more space to the private sector to expand its activities. In this context, the following statement of the Plan is noteworthy, "The industrial development strategy is being re-oriented towards enabling our vibrant private sector to reach its full entrepreneurial potential, to contribute towards production, employment and income generation. ***Unless the economic environment is conducive to high levels of private sector participation, there can be little progress in accelerating industrial development and growth.***"[4] The Plan set an ambitious target of 10 per cent per annum growth for the industrial sector while the achievement was 8.0 per cent annum.

TRENDS IN INDUSTRIAL PRODUCTION

Industrial development during the period of planning can be divided into the following distinct phases: (*i*) Phase I which covered the period of the first three plans (*i.e.* the period 1951 to 1965) laid the basis for industrial development in the future by building up a strong industrial structure; (*ii*) Phase II which covered the period 1965 to roughly 1980 was marked by industrial deceleration and structural retrogression; (*iii*) Phase III which covered the period of 1980s (1980-81 to 1990-91) was marked by industrial recovery; and (*iv*) Phase IV covering the post-reform period (*i.e.* the period 1991-92 onwards).

Phase I (1951-65): Building up of Strong Industrial Base

As noted above, Phase I laid the basis for industrial development in the future. The Second Plan, based on Mahalanobis model, emphasized the development of capital goods industries and basic industries. Accordingly, huge investments were made in industries like iron and steel, heavy engineering, and machine building industries. The same pattern of investment was continued in the Third Plan as well. As a result, as shown in Table 31.1 ***there occurred a noticeable acceleration in the compound (annual) growth rate of industrial production over the first three Plan periods upto 1965 from 5.7 per cent in the First Plan to 7.2 per cent in the Second Plan and further to 9.0 per cent in the Third Plan.*** What is significant from the point of view of long run industrial development is the fact that the rate of growth of capital goods industries shot up considerably from 9.8 per cent per annum in the First Plan to 13.1 per cent per annum in the Second Plan and further to 19.6 per cent per annum in the Third Plan. Another important group of industries from the point of view of industrial development is 'basic industries'. The rate of growth of this group also registered a significant increase from 4.7 per cent per annum in the First Plan to 12.1 per cent per annum in the Second Plan and stood at 10.4 per cent per annum in the Third Plan. This shows that a strong base for industrial development was laid during the first three plan periods. The credit for this undoubtedly goes to the massive expansion of investment that took place in the public sector.

Phase II (1965-80): Industrial Deceleration and Structural Retrogression

As shown clearly in Table 31.1, ***the period 1965 to 1976 was marked by a sharp deceleration in industrial growth.*** The rate of growth fell steeply from 9.0 per cent per annum during the Third Plan to a mere 4.1 per cent per annum during the period 1965 to 1976. It is also important to point out that even this meagre rate of industrial growth does not express the true situation as there was a sharp increase of 10.6 per cent in industrial production in the year 1976-77. If this year is left out then the rate of industrial growth over the eleven year period 1965 to 1976 declines further to a meagre 3.7 per cent per annum.[6] In a similar way, the rate of growth of 6.1 per cent per annum during the Fifth Plan owes considerably to the 10.6 per cent increase recorded in the year 1976-77. If this year is left out, the rate of industrial growth for the remaining four years comes down considerably. As is clear from Table 31.1 the last year of Phase II, *i.e.* 1979-80, recorded a negative rate of growth of industrial production of –1.6 per cent over the preceding year.

In addition to the phenomenon of deceleration in industrial growth during the period 1965 to 1980, Table 31.1 also brings out clearly the phenomenon of structural retrogression that plagued the industrial sector during this period. From the point of view of long run industrial development, the most important group of industries is the group of capital goods industries. This group registered a consistent and considerable increase from 9.8 per cent per annum in the First Plan to 13.1 per cent in the Second Plan and further to a phenomenal 19.6 per cent per annum in the Third Plan. However, in the next eleven years (1965 to 1976), the capital goods sector grew at an annual rate of only 2.6 per cent. If we consider the Fifth Plan period, the rate of growth of capital goods industries goes up to 5.7 per cent per annum but, as would be clear from Table 31.1, even this is substantially lower than the rates of growth recorded in the first three plans. The same story is found in the case of basic industries. In fact, as shown by S.L. Shetty, in the case of many industries of crucial importance, the growth between 1965-66 and 1976-77 was almost insignificant compared with the average from the previous five-year period.

Decline in the growth rate of capital goods industries and basic industries in the period after the Third Plan clearly represents the phenomenon of structural retrogression. Shetty also points out a second aspect of this structural retrogression. He shows that where growth has been moderately high, a majority of the industries belonged either directly or indirectly to elite-oriented consumption goods sector. This is illustrated by the disproportionately large increases in the output of man-made fibres, beverages, perfumes and cosmetics, commercial, office and household equipment, watches and clocks, and fine varieties of cloth.

TABLE 31.1. Annual Compound Growth Rates in Index Numbers of Industrial Production, 1951 to 1980

Use Based or Functional Classification	*1951 to 55 (4 years)*	*1955 to 1960*	*1960 to 1965*	*1965 to 1976*	*1974 to 1979 (Fifth Plan Average)*	*1979 to 80*
1. Basic Goods	4.7	12.1	10.4	6.5	8.4	– 0.5
2. Capital Goods	9.8	13.1	19.6	2.6	5.7	– 2.3
3. Intermediate Goods	7.8	6.3	6.9	3.0	4.3	1.9
4. Consumer goods	4.8	4.4	4.9	3.4	5.5	– 4.4
(*a*) Durables	–	–	–	6.2	6.8	5.6
(*b*) Non-durables	–	–	–	2.8	5.4	– 6.1
General Index	5.7	7.2	9.0	4.1	6.1	– 1.6

Source: S.L. Shetty, "Structural Retrogression in the Indian Economy since the Mid-1960s", *Economic and Political Weekly*, Special Supplement, 1978, Table 4, p. 9 and Government of India, *Hand Book of Industrial Statistics*, 1992, Table 50, p. 150 and Table 54, p. 155.

Causes of Deceleration and Retrogression.[7] Several explanations were offered for the phenomenon of deceleration and retrogression in the industrial sector during Phase II. The government expressed the view that exogenous factors such as the wars of 1965 and 1971; drought conditions in some years; infrastructural constraints and bottlenecks; and the oil crisis of 1973 were responsible for slowdown of growth. K.N. Raj argued that low growth in the agricultural sector accounted for the slowdown of industrial growth by restricting the supply of raw materials on the one hand and by constraining the demand for industrial goods on the other hand. T.N. Srinivasan and N.S.S. Narayana argued that there was a considerable slackening of real investment

in Phase II particularly in the public sector and this brought down the rate of growth in the industrial sector. A slightly different but more plausible version of the 'slackening of real investment' argument was presented by P. Patnaik and S.K. Rao according to whom there was a decline in public investment and this was followed by a decline in private investment as well due to 'the loss of stimulus' for investment. The essence of this argument is that a fall in public investment leads to a fall in private investment as well. Some economists like Deepak Nayyar, K.N.Raj and C. Rangarajan pointed to the relationship between income distribution, the demand factor and industrial growth. These economists pointed out that the market for industrial goods in the country is limited to the top 10 per cent of the population due to extreme inequalities of income and wealth. Once the demand for this section of the population gets saturated, there is no further expansion in demand. This limits the demand for consumption goods limiting, in turn, the demand for machinery and capital goods in subsequent stages. Some economists like Jagdish Bhagwati, Padma Desai, T.N. Srinivasan and Isher Judge Ahluwalia, blamed the wrong industrial policies, complex bureaucratic system of licensing, irrational and inefficient system of controls etc. for industrial deceleration.

Phase III (1981 to 1991): The Period of Industrial Recovery

The period of 1980s can broadly be termed as a period of industrial recovery. This is clearly brought out by a study of the revised Index of Industrial Production (base 1980-81). Rates of industrial growth based on this index are presented in Table 31.2.

TABLE 31.2. Rate of Growth of Industrial Production (Use-Based) During Phase III (Base 1980-81) (per cent per annum)

Use Based or Functional Classification	*1981-85*	*1985-90*	*1990-91*
1. Basic Goods	8.7	7.4	3.8
2. Capital Goods	6.2	14.8	17.4
3. Intermediate Goods	6.0	6.4	6.1
4. Consumer Goods	5.1	7.3	10.4
(*a*) Durables	14.3	11.6	14.8
(*b*) Non-durables	3.8	6.4	9.4
General Index	6.4	8.5	8.3

Source: Computed from Government of India, *Hand Book of Industrial Statistics*, 1992, Table 50, p. 50 and Table 54, p. 155.

As is clear from this table, the rate of industrial growth was 6.4 per cent annum during 1981-85, 8.5 per cent per annum during the Seventh Plan and 8.3 per cent in 1990-91. As noted by Vijay L. Kelkar and Rajiv Kumar, "This is a marked upturn from growth rates of around 4 per cent achieved during the latter half of 1960s and the 1970s. This performance is also an improvement upon the growth rates achieved during the First and Second Plan periods..."[8]

Similar trends of industrial recovery in 1980s are noted by some other economists as well. In her study spanning the period 1959-60 to 1985-86, Isher Judge Ahluwalia notes that the period 1980-81 to 1985-86 (*i.e.* the first half of the 1980s) was "marked by significant acceleration in the growth of value added in the manufacturing sector and all its use-based sectors". The value added in the manufacturing sector grew at the rate of 7.5 per cent per annum in the first half of 1980s as against only 4.7 to 5 per cent per annum in the period 1966-67 to 1979-80.[9] According to Ahluwalia, a very important aspect of the growth revival during the first half of the 1980s was that it was not associated with an acceleration in the growth of factor inputs but was, rather, based on better productivity performance. Thus, total factor productivity which registered a negative and negligible growth of -0.2 to -0.3 per cent per annum in the period 1966-67 to 1979-80 showed a marked improvement in the first half of the 1980s when it registered a growth of 3.4 per cent per annum.

It would also be useful here to consider the results of Nagaraj's study published in 1989. R. Nagaraj presented growth rates in value added in registered manufacturing for three times periods, 1959-60 to 1965-66 (period I), 1966-67 to 1979-80 (period II) and 1980-81 to 1986-87 (period III). Growth rates in value added for the three periods come out to be 7.6 per cent per annum in period I, 5.5 per cent per annum in period II and 10.4 per cent per annum in period III. This shows clearly that the industrial growth in period III was substantially higher than the industrial growth in the earlier periods. In fact, a study of the growth rates at

disaggregated level showed that growth rate in period III was higher than the growth rate in period II in all industry groups except textiles, wood and furniture, and basic metals.[10]

Causes of Industrial Recovery. The main causes of industrial recovery during 1980s are generally listed as follows :

1. New industrial policy and liberal fiscal regime. According to some economists, one of the main causes of industrial recovery during the 1980s was the liberalisation of industrial and trade policies by the government. According to Ahluwalia, "The most important changes have related to reducing the domestic barriers to entry and expansion to inject a measure of competition in domestic industry, simplifying the procedures and providing easier access to better technology and intermediate material imports as well as more flexibilty in the use of installed capacity with a view to enabling easier supply responses to changing demand conditions."[11] These factors operating from the supply side were helped by the pursuit of what may be termed as a 'liberal fiscal regime.' The important features of liberal fiscal regime were (*i*) maintenance of high budgetary deficits year after year; (*ii*) resort to massive borrowing often at high interest rates, and (*iii*) the encouragement of dissaving. All these aspects of liberal fiscal regime helped to expand the demand for manufactured goods in the economy.[12]

The above discussion shows that while liberal fiscal regime helped in generating demand for manufactured goods, liberal industrial and trade policies ensured that an adequate 'supply response' was forthcoming.

2. Contribution of the agricultural sector. According to some economists, increased prosperity of large farmers in certain regions of the country helped in creating additional demand for industrial goods. According to R Thamarajakashi , the rural sector's demand for non-agricultural consumer products rose considerably from 35 per cent in 1967-68 to 47 per cent in 1983. Not only this. There was a spurt in demand for a certain range of manufactured goods due to increase in the use of manufactured inputs per unit of cultivated area (or output). As shown by Thamarajakashi, the percentage of purchased inputs to total inputs (taken as a proxy for demand for industrial inputs in agricultural production) roughly doubled from 16.4 per cent in 1970-71 to 35.6 per cent in 1983-84.[13]

3. Growth of service sector. There was a significant increase in government expenditure on all services in the 1980s. The consumption pattern of the service class is less food-intensive and more oriented towards durable consumer goods. Therefore the consumption pattern of effective demand in 1980s changed in favour of consumer durable goods. As a result, consumer durables were pushed to the "forefront of growth." Fast growth of the consumer durable goods sector pushed up the rate of industrial growth.

4. The infrastructure factor. There was a marked resurgence in infrastructure investment in 1980s. As against only 4.2 per cent per annum increase in infrastructure investment during 1965-66 to 1975-76, the increase was as high as 9.7 per cent per annum during 1979-80 to 1984-85. Infrastructure investment rose further by 16.0 per cent in 1985-86 and 18.3 per cent in 1986-87. According to Ahluwalia, this revival of investment in the infrastructure sectors in the 1980s was also accompained with a discernible improvement on the efficiency front.

Phase IV (The Period 1991-92 Onwards)

The year 1991 ushered in a new era of economic liberalisation. Major liberalisation measures designed to affect the performance of the industrial sector were — wide-scale reduction in the scope of industrial licensing, simplification of procedural rules and regulations, reductions of areas exclusively reserved for the public sector, disinvestment of equity of selected public sector undertakings, enhancing the limits of foreign equity participation in domestic industrial undertakings, liberalisation of trade and exchange rate policies, rationalisation and reduction of customs and excise duties and personal and corporate income tax, etc. Trends in industrial growth in this period (known as the post-reform period) are given in Table 31.3.

For purpose of analysis, it is better to divide the post-reform period into two sub-periods: (*i*) the period of 1990s (upto 2001-02, i.e. upto the end of Ninth Plan), and (*ii*) the period 2002-03 to 2006-07 (*i.e.* the period of Tenth Plan).

The Period of 1990s. Important facts regarding industrial growth trends in the period of 1990s are as follows :

1. The average annual growth rate of industrial production which was 7.8 per cent in the pre-reform decade (1980-81 to 1991-92) fell to 5.7 per cent during the period 1990-91 to 1999-2000.