MASTER OF BUSINESS ADMINISTRATION

MBA-105

BUSINESS ENVIRONMENT

Directorate of Distance Education
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CONTENTS

Course: Business Environment	
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Business Environment and Type of Business Environment

STRUCTURE

1.0 Learning Objectives

After going through this lesson, the learner should be able to:

- Explain nature of Business.
- Explain the concept of business environment

- Describe the nature and scope of business environment
- Describe the importance of business environment
- Explain the components of business environment
- Discuss the relationship between business environment and strategic management

1.1 Introduction

Business is an organisation or enterprise engaged in producing goods and services for profit motive. It is a collective effort where a firm is engaged in commercial, industrial or professional activities. The main aim of business is to satisfy the needs of customers. The success of every business depends on adapting itself to the environment within which it functions. For example, with changes in the government policies, the business needs to adapt itself with the new policies. Similarly, any technological advancement may render the existing products obsolete, such as the introduction of smart phones has replaced the telephone to a greater extent. Therefore, it is very important to have a clear understanding of the basic concept of business environment and the nature of its various components.

Business Environment is sum or collection of all internal and external factors such as employees, customer's needs and expectations, supply and demand, management, clients, suppliers, owners, activities by government, innovation in technology, social trends, market trends, economic changes, etc. These factors affect the function of the company and how a company works directly or indirectly. Sum of these factors influences the companies or business organisations environment and situation. Business Environment consists of all those factors that have a bearing on the business, such as the strengths, weaknesses, internal power relationships and orientations of the organization; government policies and regulations; nature of the economy and economic conditions; socio-cultural factors; demographic trends; natural factors; and, global trends and cross-border developments.

A business firm is an open system. It gets resources from the environment and supplies its goods and services to the environment. There are different levels of environmental forces. Some are close and internal forces whereas others are external forces. External forces may be related to national level, regional level or international level. The environmental forces provide opportunities or threats to the business organization. Every business organization tries to grasp the available opportunities and face the threats that emerge from the business environment. Business organizations cannot change the external environment but they just react/ adjust according to the external environment. They change their internal business components (internal environment) to grasp the external opportunities and face the external environmental threats. It is, therefore, very important to analyze business environment to survive and to get success for a business in its industry. It is, therefore, a vital role of managers to analyze business environment so that they could pursue effective business strategy. A business firm gets human resources, capital, technology, information, energy, and raw materials from society. It follows government rules and regulations, social norms and cultural values, regional treaty and global alignment, economic rules and tax policies of the government. Thus, a business organization is a dynamic entity because it operates in a dynamic business environment.

The word 'Business Environment' has been defined by various authors as follows:

According to **Keith Davis**, "Business environment is the aggregate of all conditions, events and influences that surround and affect it".

According to **Reinecke** and **Schoell**, "the environment of business consists of all those external things to which it is exposed and by which it may be influenced directly or indirectly.

1.2 Nature of Business

Business may be understood as the organized efforts of enterprise to supply consumers with goods and services for a profit. Businesses vary in size, as measured by the number of employees or by sales volume. But, all businesses share the same purpose: to earn profits.

The purpose of business goes beyond earning profit. There are:

- It is an important institution in society.
- Be it for the supply of goods and services.
- Creation of job opportunities.
- Offer of better quality of life.
- Contributing to the economic growth of the country.

Hence, it is understood that the role of business is crucial. Society cannot do without business. It needs no emphasis that business needs society as much.

These definitions give a clear understanding of the business environment. We can say that business environment is a combination or mixture of complex, dynamic and uncontrollable external factors within which a business is to be operated.

The change in tastes and preferences of customers, introduction of new technologies, innovations, government policies, etc., all are parts of the business environment. Business needs to accept and adapt these changes promptly to survive in the market. So, it is necessary for the business to analyse the business environment

1.3 Businesses in Today's Environment

Modern business is dynamic and customer oriented. If there is any single word that can best describe today's business, it is change. This change makes the companies spend substantially on Research and development (R & D) to survive in the market. Mass production and mass marketing are the norms followed by business enterprises. The number of companies with an annual turnover of Rs.100 crore each was only three in 1969-70.The figure has manifold these days.

Today's business is characterized by diversification, which may be:

- **Concentric Diversification** - It refers to the process of adding new, but relates products or services.
- **Horizontal Diversification** - Adding new, unrelated products or services for present customers is called horizontal Diversification.
- **Conglomerate Diversification** - It refers to adding new and unrelated products or services. Going international is yet another trend followed by modern business houses.

Business houses are exposed to global competition, which argues well for consumers. Also occupying a major role is science in the global economic scenario.

1.4 Nature of Business Environment

The business environment of an organisation usually poses threats as well as opportunities. To grasp the opportunities and reduce the threat, it is important to know the nature of business environment. Following are some points which describe nature of business environment:

- **Internal and external environment:** Every business is surrounded by internal and external environment. Internal environment can be controlled by an organisation, like men, money, material, machine and method, whereas external environment is uncontrollable like political conditions, technologies, legal regulations, etc.
- **Dynamic and ever-changing**: Business environment keeps on changing frequently in terms of technologies, government rules and regulations, socio-economic conditions, etc., which make business dynamic.
- **Complexity of the environment:** Business environment cannot be easily analysed because of too much complexity involved. Environment consists of a number of factors, events, conditions and influences, generating from different sources which impact business, thus, making the business complex.
- **Inter-relatedness:** Factors of business environment are related to each other. For example, change in political parties will result in changing the government

rules, fiscal policies, market conditions, technology, etc. So, all the factors need to be scanned properly because these factors are inter-related to each other.

- **Uncertainty:** It is difficult to predict the changes going to take place in future because environment keeps on changing. These changes are uncontrollable. So, business can only try to combat from these challenges. For example, in case of fashion industries, changes take place so frequently, economy could collapse any time.
- **Impact:** Impact means the effect of environment on business. Business environment has both long-term and short-term impacts on business. For example, different firms may get influenced differently from change in monetary policy.
- **Inter-dependence:** A business firm and its environment are mutually interdependent. The economic status of a country affects the development of technology or it may change the lifestyle of people.

1.5 Scope of Business Environment

The aspects which fall under the scope of business environment are as follows:

- **Internal and external environment**: Internal environment includes all those factors that are within an organisation and impart strength or cause weakness in business. For example, inefficient human resource, superior raw material, etc. External environment includes those factors which are beyond the control of business and are outside the organisation. They provide opportunities and pose threat to business. For example, change in political conditions, technological change, etc.
- **Specific and general environment:** Specific environment includes external forces that directly impact or influence organisations' decisions and actions and are directly relevant to the achievement of organisations' goals. The main forces that make up the specific environment are customers, suppliers,

competitors and pressure groups. General environment includes the economic, political/legal, socio-cultural, demographic, technological and global conditions that affect organisations. External forces do not affect organisations to a great extent, but organisations must plan, organise, lead and control their activities taking into account these factors.

- **Micro environment and macro environment:** Micro environment impacts the working of a particular business. It has direct impact on business activities. It includes customers, suppliers, market intermediaries, competitors, etc. These factors are controllable to some extent. Macro environment is general environment that impacts the working of all businesses. It is uncontrollable and influences indirectly and includes political conditions, economy, technology, etc., come under macro environment.
- **Controllable and uncontrollable environment:** All those factors which are governed by business come under controllable environment. Internal factors are treated as controllable factors, like men, material, machine, money, etc. Uncontrollable factors are external and are beyond the control of business like technological change and law related change.

1.6 Importance of Business Environment

Following points describe the importance of business environment:

- **Identification of business opportunities:** Many opportunities are provided by business environment to the organisation. Scanning business environment would help business get the first mover advantage. If changes are analysed carefully, then they can be the reason for business success.
- **Optimum utilisation of resources:** Resources like raw material, machine, money, labour, etc., are input for business. All these inputs are provided by environment to the business firms for carrying out their activities and also expect something in return.

- **Identification of threat and early warning signal:** Business can recognise the threat by analysing the change taking place in the environment. For example, if any new multinational company is entering the Indian market, the manager of an Indian firm dealing with same product as that of the multinational company should take it as a warning signal. Before the MNC launches its product, the manager should implement measures, such as improving the quality of his product and heavy advertisement.
- **Coping with the rapid changes:** To efficiently cope with these changes, managers must understand the environment and should adopt appropriate courses of action at the right time. It helps management become more sensitive to ever-changing needs of customers. As a result, they are able to respond to such changes effectively.
- **Meeting competition:** This helps firms analyse competitors' strategies and formulate their strategies accordingly.
- **Identifying firm's strength and weakness:** Business environment helps identify the individual strength and weakness in view of the technological and global developments.
- **Assisting in planning and policy formulation:** Business environment brings both threats and opportunities to a business. Having a good understanding of the business environment can immensely help an organisation's management in their future planning and decision-making endeavours. For example, competition increases with the entry of new firms in the market.

The management has to draft new plans and policies to deal with new competitors. Environmental awareness provides intellectual stimulation to planners in their decision making. They can make changes in their plans efficiently and effectively.

1.7 Components of Business Environment

The performance of an organisation is affected by the business environment. It has a far-reaching impact on its survival, profit and growth. There are certain forces inside and outside the organisation. These forces affect the business both in positive and negative ways. The components of business environment are explained below with the help of a diagram:

Components of Business Environment

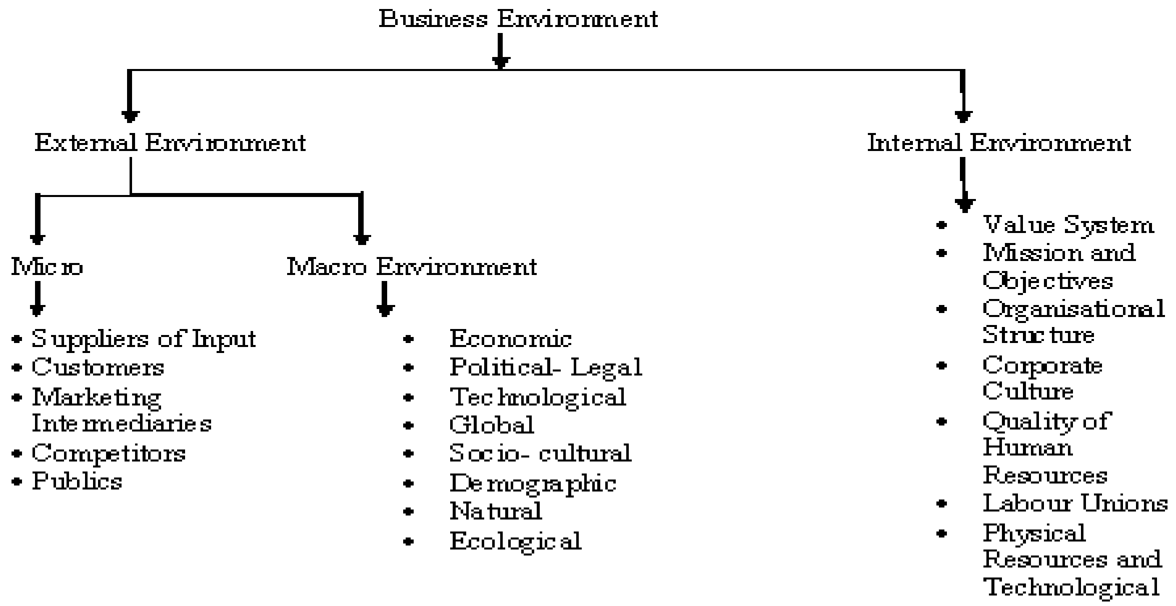

Fig: Components of Business Environment

Internal environment: The factors or conditions that exist within an organisation and affect its performance. These factors are controllable in nature and organisation can try to change or modify these factors. Organisation's resources like men, material, money, method and machine come under internal environment. Various internal factors are as follows:

- **Value system:** The values are the ethical beliefs that guide the organisation in achieving its mission and objectives. It is framed by top-level managers like board of directors. The extent to which the value system is shared by all in the organisation is an important factor contributing to its success.
- **Mission and notes objectives:** The objective is the end towards which business activities are directed. All businesses focus on maximisation of profit.

Mission is defined as the overall purpose or reason for its existence. A mission guides and influences an organisation's decisions and economic activities. An organisation can change or modify its mission and objective accordingly.

- **Organisation structure:** The organisational structure is the hierarchy in business that define roles, responsibilities and supervision. The composition of the board of directors, the professionalism of management, etc., comes under organisation structure and are important factors influencing business decisions. For efficient working of a business organisation and to facilitate prompt decision making, the organisation structure should be conducive.
- **Corporate culture:** Shared values and belief in an organisation which determine its internal environment are called corporate culture. Organisation where there is strict supervision and control results in lack of flexibility and unsatisfied employees. The sets of values that help members understand what organisation stands for how it does work, what it considers, cultural values of business forces of business, and so on. It helps in direction of activities.
- **Human resources:** Human quality of a firm is an important factor of internal environment. Skills, qualities, capabilities, attitude, competencies and commitment of its employees, etc., could contribute to the strengths and weaknesses of an organisation. Organisations may find it difficult to carry out modernisation and redesigning because of resistance by its employees.
- **Physical resources and financial capabilities:** Physical resources, such as plant and equipment, facilities and financial capabilities of a firm determine its competitive strength which is an important factor for determining its efficiency and unit cost of production. Also research and development capabilities of a company determine its ability to introduce innovations which enhance the productivity of workers. Financial capabilities are company's source of fund generation.
- **External environment:** The factors and the conditions which are outside the organisation and affect the performance of business. External factors are

further divided into micro environment and macro environment which are as follows:

- **Micro environment:** Those factors which have direct impact on business. The various constituents under micro environment are as follows:

- **Suppliers of inputs:** The suppliers of inputs are important factors in the external micro environment of a firm. Suppliers provide raw material and resources to the firm. A firm should have more than one supplier for proper inflow of inputs.
- **Customers:** These are the buyers of firm's products and services. Customers are an important part of external micro environment because sales of a product or service are critical for a firm's survival and growth, so it is necessary to keep the customers satisfied.
- **Marketing intermediaries:** Intermediaries play an essential role of selling and distributing its products to the final customers. Marketing intermediaries are an important link between a business firm and its ultimate customers. Retailers and wholesalers buy in bulk and sell business products and services to the ultimate consumer.
- **Competitors:** Competitors are the rivalry in business. Competition can based on pricing of products or based on competitive advertising. For example, organisations may sponsor some events to promote the sale of different varieties and models of their products. Business formulates strategies after analysing their competitor.
- **Public:** Public or groups, such as environmentalists, media groups, women's associations, consumer protection groups, are important factors in external micro environment. According to Philip Kotler, Public, is any group that has an actual or potential interest in or impact on the company's ability to achieve its objective.

Macro Environment: These are the factors or conditions which are general to all businesses and are uncontrollable. Because of the uncontrollable nature of macro forces, a firm needs to adjust or adapt it to these external forces. These factors are as follows:

- **Economic environment:** All those forces which have an economic impact on businesses are called economic environment. It includes agriculture, industrial production, infrastructure, and planning, basic economic philosophy, stages of economic development, trade cycles, national income, per capita income, savings, money, etc., For example, low per capital income will negatively impact business because people have less money to spend.
- **Political-legal environment:** The activities of legislature, executive and judiciary play a vital role in shaping, directing, developing and controlling business activities. Rules and regulations, framed by the government, like licensing policy, polythene ban, etc., affect the business. Business growth can be achieved by using a stable and dynamic political-legal environment.
- **Technological environment:** Systematic application of scientific or other organised knowledge to practical tasks or activities is called technology. As it is changing fast, businessmen should keep a close look on those technological changes for its adaptation in their business activities.
- **Global or international environment:** The global environment is also important for shaping business activity. In the era of globalisation, whole world is a market. Business analyses international environment to cope up with the changes.
- **Socio-cultural environment:** People's attitude towards work and wealth, lifestyle, ethical issues, role of family, marriage, religion and education and also social responsiveness of business affect the business.
- **Demographic environment:** Population size and growth, life expectancy of the people, rural-urban distribution of population, the technological skills and educational levels of labour force come under demographic environment. These features also affect the functioning of organisations.

- **Natural environment:** The natural environment plays an important role as it provides raw materials and energy for production in a firm. Natural environment consists of geographical and ecological factors such as minerals and oil reserves, water and forest resources, weather and climatic conditions and port facilities. These are very important for many business activities. For example, in places where temperatures are high, the demand for coolers and air conditioners is high. Also, demand for clothes and building materials depends on weather and climatic conditions. Natural calamities like floods, droughts, earthquakes, etc., immensely affect business activities.

1.8 Relation between Business Environment and Strategic Management

The set of decisions and actions that result in the formulation and implementation of plans designed to achieve a company objectives are called strategic management. Strategic decisions are based on what a manager forecasts rather than what he knows. Strategic decisions have complex implications for more areas of the firm. The characteristics of strategic management decisions vary with the level of strategic management activity.

- Strategic management helps in defining the objectives and policies for the business. To make strategy, a business needs to scan its environment.
- In formulating a strategy, the strategic decision makers must analyse internal as well as external conditions in the environment, which are described in the following sections:
- The analysis of internal and external environment will help managers determine what goals and mission they can or should adopt, and the strategic options that are available.
- Strategic planning should be based on business environment analysis. The world today is changing at a rapid pace. So it is very important for companies to scan the business environment more clearly, and make up strategic planning that can match the changes.

- The environment is changing, and the strategy which is suitable for companies today may bring threat tomorrow. Strategy is effective only if it is flexible.

1.9 Check Your Progress

1. ___________________ is the aggregate of all conditions, events and influences that surround and affect it.
2. All those factors which are governed by business come under controllable environment. **(True/False)**
3. A business firm and its environment are mutually ___________________.
4. _______________ and ________________ are the two types of external environment.
5. **Which among the following comes under economic environment?**

- Education
- Population size
- GDP
- Lifestyle

1.10 Summary

- Business environment is a combination or mixture of complex, dynamic and uncontrollable external factors within which a business is to be operated.
- Business environment is complex, uncertain, inter-related, dynamic and interdependent.
- Specific environment includes external forces that directly impact or influence organisations' decisions and actions and are directly relevant to the achievement of organisations' goals.
- General environment includes the broad economic, political/legal, socio-cultural, demographic, technological and global conditions.
- Business environment helps in identifying opportunities and threats.

- The components of business environment are: internal and external environment. External environment consists of micro and macro factors which affect the business.
- The set of decisions and actions that result in the formulation and implementation of plans designed to achieve a company objectives are called strategic management.
- Strategic management helps in defining the objectives and policies for the business. To make a strategy, a business needs to scan its environment.

1.11 Key Words

Business Environment: Business environment is a combination or mixture of complex, dynamic and uncontrollable external factors within which a business is to be operated.

Opportunities: The favourable conditions which can give a positive outcome.

Threats: The unfavourable conditions which can give a negative outcome.

Globalisation: An integration of economies, industries, markets, cultures and policy-making around the world.

Strategic management: The set of decisions and actions that result in the formulation and implementation of plans designed to achieve an organisation's objectives.

1.12 Self Assessment Test

1. Describe the forces which affect individual enterprises directly and immediately in their day-to-day working.

2. Explain how the understanding of business environment helps the management in coping with the rapid change and identifying opportunities and threats.

3. ABC Pvt. Ltd. was operating its business in USA. The company started exporting its product to India with the introduction of New Industrial Policy in 1991. The company appointed retailers in India who had direct links with suppliers to replenish

stocks when needed. Identify and explain the dimensions of business environment discussed above.

4. Strategic decisions are based on what a manager forecasts rather than what he knows. Explain the relationship between strategic management and business environment**.**

1.13 Answers to Check Your Progress

1. Business Environment

2. True

3. Interdependent

4. Micro environment; macro environment

5. GDP

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Course: Business Environment	
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Environmental Scanning And Risk Assessment

STRUCTURE

2.0 Learning Objectives

After going through this lesson, the learner should be able to:

- Know the meaning of environmental screening
- Explain the importance of environmental screening
- Discuss the steps of business environmental analysis
- Describe the techniques of environment analysis i.e. ETOP, SWOT, and PESTLE etc.
- Describe the SWOT technique of business environmental analysis
- Explain the meaning of risk
- Explain how organisations assess risk

2.1 Introduction

An organisation operates within a particular environment which is comprised of internal and external environments. The internal environment of an organisation includes its employees, its policies that exist in the organisation, its strategy, its mission, etc. The internal environment is responsible to reflect the common purpose of the organisation. The external environment includes government, regulating agencies, customers, and suppliers, public at large, etc. which affect the business strategy of the organisation. Internal environment is managed internally by the key persons of the organisation. Thus, it is important for a organisation to screen the external environment in detail to make a strategy that could work for it. SWOT technique is used to make a complete analysis of internal and external environment of an organisation. In this lesson, you will be able to know the meaning and importance of environmental screening, analysis of business environment and SWOT analysis in detail. Towards the end of the lesson, risks in business environment have been discussed.

2.2 Meaning And Importance Of Environmental Screening

The term 'environment' means surroundings near you, which includes all components of environment like physical environment, social environment and governing environment. Physical environment consists of plants, land, water and all natural resources. Social environment consists of labourers, staff, management, suppliers, customers or all other human resources. Governing environment are rules, regulations and policies of the government. The term ‘screening’ means the process of evaluation or assessment of anything with the purpose of gathering data on any subject matter and coming to a conclusion. Thus, it may be concluded that environmental screening is a process in which an organisation makes assessment or analysis of all the components of the environment and screens their impact on its functioning, stability, growth and profits. For an effective environmental screening, an organisation must follow the following steps:

1. Defining the type of business: First, the organisation should assess what type of business it is dealing in and later on decide how environment will impact it. The same environment affects the clothing business and food business differently.

2. Defining the scope of project: If screening is done for a particular project, then it is necessary to define the scope of the project. The scope will decide how environment will affect the project of the organisation.

3. Defining the type of environment: It is important to define what type of environment an organisation is working in. It is important to consider all types of components of environment, such as physical, social or governing, and how the business will be affected due to them.

4. Preparing a report: A detailed report should be made on how the organisation will be affected by the surrounding environment.

5. Monitoring: Environment is not a static thing. It keeps on changing its features and characteristics. For example, employees keep on changing their jobs, customers keep on changing their choices, government keeps on changing its policies, etc. Thus, environment and its impacts should also be constantly monitored.

If an effective environmental screening is done properly, then it gives following benefits:

- It gives the clear picture of what kind of environment the organisation is working in. Also, the organisation becomes aware of the features of different components of environment.
- Organisation gets the idea of opportunities and threats possible in the environment.
- Organisation is able to define the scope of its business, like how much the organisation can grow and to what extent it can raise its targets and profits.
- Organisation becomes aware of the existing and possible competitors.
- Continuous monitoring of environment makes an organisation aware of the upcoming dangers and updates for future challenges. This makes an organisation aware of its customers' choices, so that the organisation could further improve the quality of its products or services.

2.3 Business Environmental Analysis

The environmental analysis process is not a static process. It is rather a dynamic process which may change from one business to another. For example, the business process analysis would be different for the airline services to that of the beauty salon services. A business manager plays a vital role in the analysis of business environment which needs to thoroughly understanding the availability of opportunities and possible threats. As per the analysis, an organisation needs to work on the available opportunities as per its strength and weakness.

Following are four basic components of business environment analysis:

- **Scanning:** The term 'scanning' means analysing all parts or components of anything in order to develop some features of that thing. Being the first component of the environmental analysis process, this analyses the environmental factors of an organisation. The purpose of scanning is as follows:

(i) Scanning helps in identifying the possibilities of environmental changes which may affect the working of an organisation.

(ii) Understanding the present changes in the environment.

Scanning is basically a non-structured activity. This is because the data in scanning is unlimited, but is ambiguous and imprecise in nature. So, it is difficult to distinguish what data is relevant or what is not. For the environmental analysis process, it is the basic challenge to extract the relevant data and make the best use of it.

- **Monitoring:** 'Monitoring' means keeping a constant eye or check on something. Thus, in environmental analysis, monitoring keeps a check on environmental changes from time to time. For example, employees keep on changing, natural resources keep on changing, and government and their policies keep on changing. Thus, after scanning, it is necessary to keep monitoring what sort of changes the concerned environment is facing and what impact it might cause on the normal functioning of the organisation. Constant monitoring ensures that businesspersons are aware, and make responses towards the possible change in the business environment.
- **Forecasting:** Scanning and monitoring are steps on those aspects which have already happened and organisation cannot change them. These are sunk aspects, i.e., which have already taken place in the past and will not change in the future. But when an organisation is formulating a strategy for its operations, it might require future prospects and future orientation too. Forecasting is, thus, making any predictions about future and is, consequently, a part of business environment analysis. Forecasting can be done for any business-related project or aspect. For example, a forecasting can be made about whether a particular technology will arrive in the market or not,

what would be the government's new policies regarding tax, whether customers would change their preferences or would they like the innovation in the products or services, etc. These kinds of questions are being attempted to be answered in forecasting. Scanning and monitoring are comparatively easy tasks than forecasting. Forecasting is a complex task which requires brainstorming with which future predictions are being made. The scope of forecasting is more specific and clearer than monitoring and scanning. The results of monitoring and scanning are accurate as study of something present is done. But results of forecasting are contingent in future.

- **Assessing:** After scanning, monitoring and forecasting the business environment, organisation must make proper evaluation or assessment of collected data in the above-mentioned steps. The organisation also needs to analyse what impact it will create on functioning.

Assessment will provide answer to the following questions:

(i) What strategy needs to be made for the smooth functioning of the organisation?

(ii) What changes might an organisation want to bring in your current strategy?

(iii) What alternatives does an organisation have in case of negative changes in environment?

(iv) How will an organisation face the coming changes?

2.4 Steps In Business Environmental Analysis

Following steps need to be followed in the process of business environmental analysis:

A. Scanning all the required components

B. Grouping the scanned components

C. Observing the internal components

D. Monitoring the external components

E. Outlining variables for analysis

F. Usage of different techniques for analysis

G. Forecasting future outcomes

H. Formulating strategies

I. Execution of formulated strategies

J. Monitoring

Let us discuss the above-mentioned steps in detail:

A. **Scanning all the required components**: Environment of an organisation consists of various components. But, not all factors and aspects would be equally important or even important for the functioning of an organisation. A good strategist always distinguishes the relevant factors and scans them in detail. He/she looks for all the required components of environment and would study the relevant factors in detail. This way, he/she collects the required components and would present a scanned report.

B. **Grouping the scanned components:** In the first step, the required raw information is gathered. In this step, the collected components are to be grouped; for example, what is affecting the stability, what is affecting the sales, what is affecting the growth, etc. Grouping is made of all the collected information.

C. **Observing the internal components:** After scanning and grouping the relevant components of external environment, the strategist looks at the internal components of the organisation. For example, how the employees are reacting to the environmental changes and how smooth an organisation is functioning as the external components change in the environment.

D. Monitoring external components: As an environment is not static in nature, it keeps on changing, for example, changing in government policies, changing in customer's preferences, changing in supplier's rates, etc. Thus, just one-time scanning is not a fruitful activity for the organisation. An organisation needs to constantly monitor and make aware of the upcoming changes.

E. Outlining variables for analysis: Variables are the components responsible for bringing a change in an external environment. Some variables are national minimum wage, GDP, tax policies, competitors' policies, customers' preferences, etc. A strategist must outline all such variables and study them from time to time, so that he could bring the necessary change in the functioning.

F. Usage of different techniques for analysis: Different techniques are being used for a proper environmental analysis, such as benchmarking, scenario building, network methods, etc. The term 'benchmarking' means setting the best standard as per the industry and then comparing company's performance with the set standards. Scenario building is presentation of overall picture of the system of an organisation along with the affecting components. Network method is a complex process which is used to analyse the external environment of the organisation. This method helps in analysing the available opportunities in the market and studying possible threats. A network method also judges how internal strengths and weaknesses will be affected by the external environment. Essential data can be gathered through Delphi method, conceptualising, study and verifiable enquiry method.

G. Forecasting future outcomes: In a business environment analysis, it is necessary to make predictions for future outcomes. A good strategist will always make future predictions of how the environmental components may affect the functioning of the organisation. The assessment of past results can also be made in this step.

H. Formulating strategies: It is also one of the important steps of business environmental analysis. After the assessment of all the above environmental components, an organisation formulates the required strategies for the functioning. As you have already studied above, conduct the SWOT analysis before making an effective strategy. SWOT analysis means analysing the strengths, weaknesses, available opportunities and possible threats of the organisation. There are various ways of formulating or designing a strategy. Internal or core components are being recorded in Strategic Advantages Profiles (SAP). However, external components are being recorded in Environmental Threat and Opportunity Profile (ETOP). Both SAP and ETOP profiles can be compounded into SWOT profile. To evaluate internal and external components, External Factor Evaluation (EFE) matrix is being used by the strategists as a tool.

I. Execution of formulated strategies: After the above steps, a strategist implements and executes upon the formulated strategies. The strategist always evaluates how he had formulated the given strategy and how that can be effectively implemented. He/she also makes the required future predictions. This process is also often referred to the process of SWOT analysis

J. Monitoring: The strategist must keep monitoring the external environment. As an environment keeps on changing, thus, it is necessary to have a continuous look at the changes and bringing the required changes in the plan or strategy.

2.5 Techniques Of Environmental Analysis

1. SWOT analysis

SWOT analysis refers to the analysis of both the internal and external environments of an organisation. In this term, S stands for Strengths and W stands for Weaknesses. Both these terms are internal components of an organisation. O stands for available Opportunities in the market and T stands for the possible Threats in the market. Both of these are the external components of the organisation.

- **Strengths:** The term 'strengths' basically means the things you are good at or your capabilities. In the organisational context, it means the core competencies or capabilities of an organisation for which it can gain strategic advantages from its competitors. Even if it does not gain any advantages over competitors, it refers to an organisation's capacities in which the organisation is having affirmative aspects. Strength is necessary for every organisation to gain competitive advantages. For example, some organisations have their employees as their strength and some organisations may have low cost of production as their strength.

- **Weaknesses:** Weaknesses are exact opposites of Strengths. While strengths are competitive advantages, weaknesses are competitive disadvantages of an organisation. Weaknesses are responsible for downfall of an organisation. The term 'weakness' also refers to the things in which the organisation is not good. For example, an organisation might not have better marketing strategies in comparison to its competitors. Then, in such a case, marketing would be its weakness. □□
- **Opportunities:** The term 'opportunity' means a chance to grab on in a positive sense. This is actually a favourable condition or circumstances present in the external environment, which should be grabbed by the organisation, in order to increase its strengths and gaining competitive advantages. A company's strategist must be aware of the coming opportunity in the market, so that it could grab them on time and could raise revenues and profits; for example, sudden rise in demand of customers, new government policies in the favour of the organisation, emerging technologies, etc. □□
- **Threats:** The term 'threat' means exposing vulnerability of something which might create an adverse impact. In an external environment, if suddenly or even gradually some changes occur and those are not in favour of the organisation, then these are called threats to the organisation. For example, a changes in preferences of customers, and changes in government policies, which are not in favour of the organisation, are considered as threats to the organisation.

It is not necessary that an organisation has only its one single strength. An organisation might have one or more strengths at one time. More number of strengths would give an organisation more competitive advantages. An organisation might have one or more weaknesses which would degrade its competitive position in the market. The weakness of an organisation would factually hamper the growth of an organisation. The strengths and weaknesses of an organisation could be collectively determined and this combination would create a collective impact on the organisation and it is called a circumstance of synergistic effect. The concept of synergy says that if two things are merged together, then the resulting effect could be greater or lesser. This means when strengths and weaknesses of a company are understood together, then they could create a resulting strength or resulting weakness. This could be better understood as ‘two plus two could be either five or three’.

The SWOT analysis is a tool to evaluate the strengths, weaknesses, opportunities and threats of an organisation. Every organisation must do this analysis very effectively, as all these areas are necessary to be understood in detail. A strategy would be formed on the basis of these elements only. Through SWOT analysis, a detailed study could be done about both internal and external factors of an organisation.

2. ETOP analysis

ETOP is a device that considers the environmental information and determines the relative impact of threats and opportunities, for the systematic evaluation of environmental scanning. This analysis divides the environment into different sectors and then analyses their effect on the organization.

3. QUEST analysis

QUEST analysis was proposed by B. Nanus. It is a four-step process that uses scenario writing for environmental scanning. The four steps involved in this technique are as follows:

- Strategy planners first observe the events and trends of the organization.
- From the first observation, they broadly consider important issues that may affect the organization, using environment appraisal.

- A report is created by summarizing these issues, their effects and different scenarios to show the implementation of these strategies.
- In the last step, reports and scenarios are reviewed by the planners to decide the feasibility of the suggested strategies that are beneficial for the organization.

4. PESTLE analysis

PESTLE is an acronym and it is used as an analytical tool. It stands for the Political, Economic, Social, Technological, Legal and Environmental factors which influence the business environment of an organization.

- It helps in identifying the environmental factors that affect the strategies of the organization. However, it is not necessary that the environmental analysis provides valuable information to the organization. Hence, it becomes important for the organization to go in for a more quantitative approach to get the real data for organizational goals.
- PESTLE analysis helps in identifying the key factors of business and their differential impact on the organization. It also helps in determining the extent to which these factors affect the competitors of the organization. The three key external factors that affect the organizations include short life-span of technology, convergence of customer requirements and access to the resources available globally.

2.6 Assessing Risk In A Business Environment

The term ‘risk’ means a situation or circumstance where there is an exposure to danger. Business risk, therefore, means when an organisation is exposed to danger or threat, which could lower its profits or which may hamper the achievement of its targets. Any threat which may harm the normal functioning of an organisation is known as business risk. Any exposed risk could affect the organisation in the following ways: □□

- It could disrupt normal working.
- It could create an adverse effect on sales or revenue.
- It could defame the brand image.
- It could create an adverse impact on growth.

It is not factually correct every time to blame managers or staff for the risk. A risk to business occurs because of many reasons. Following are the reasons which may cause a business risk:

- Preference of customers, their demand and sales
- Overall per unit cost to the company
- Existing competition in the market
- Economic climate
- Government policies, rules and regulations.

Assessing risk means making an estimate of what level of risk is present in the given business situation. Thus, risk assessment is actually risk measurement. Following steps are to be taken to assess risk:

1. **Define the type of risk:** There are various types of risks that are present in the market, to which a business is exposed. The first step is to identify the types of risks that are present. There are following types of risks present in the market:

- **Financial risks:** Financial risks are risks which affect the financial or monetary position of an organisation. Financial risks include credit risk, liquidity risk, asset-based risk, foreign investment risk, equity risk, currency risk, etc. In these types of risks, the organisation faces money crisis.
- **Marketing risks:** When an organisation fails to make a better marketing strategy for its products or services, it faces such types of risks. These include a failure of marketing of products or services, risk, risk related to product development, product pricing, product promotion, etc.
- **Operational risks**: When an organisation fails to properly operate its day- to-day functioning, it is known as operational risk. In these kinds of risks,

employees are not able to work properly for the organisation. For example, risk of electricity cut off, risk of disruption in the Internet, etc.

- **Strategic risks:** When there is a failure in proper strategy making or when strategy is not updated as per the changes in the environment, such situation is known as strategic risk; for example, failure of management in adapting new technology, failure in meeting customers' demands, etc.
- **Workforce risks:** When the workforce of the organisation does not perform its duties well or does not work for the organisation, it is known as workforce risks; for example, strike of labourers, continuous absence of labourers or employees, etc.

2. Estimate the likelihood of occurring: After analysing all types of risks an organisation needs to estimate what are the fair chances of each risk occurring in the future. Various techniques like percentages or probability can be used to estimate the chances of occurrence of risk. For example, there are twenty-five percent chances that the demand is going to fall down in the coming time for the said project.

3. Estimate the loss: After identifying the risks, the organisation has to estimate the chances of its occurrence and the extent of loss it may cause to the organisation. For example, there are twenty-five percent chances that the demand may fall for the said project and, consequently, the organisation may suffer loss of revenue of one million rupees in one month of time.

4. Decide whether or not to take the risk: The organisation has come to a rough figure of how much loss it is going to suffer if the risk proves to be right. Organisation takes decision whether or not that risk is worthy to take. In the above example, there are seventy-five percent chances that the demand would not fall and if the demand rises, the organisation would have profit of ten million rupees in the coming month. So, considering all these factors, project is worthy to be taken.

2.7 Check Your Progress

1. In following options, what is an opportunity for a business?

A. A business has poor marketing strategies

B. A business has a good labour force

C. A business is exposed to a low demand for its products

D. A business can have a high demands of its products in the coming future

2. Out of the following options, which one is strength of a business?

A. A business has poor marketing strategies

B. A business has a good labour force

C. A business is exposed to low demand of a product

D. A business can have high demand of its product in the coming future.

3.________ is a situation of exposure to danger.

4. Failure to adapt to a new technology is ________ risk.

2.8 Summary

- Environmental screening is a process in which an organisation makes an assessment or analysis of all the components of the environment and screens their impact on its functioning, stability, growth and profits.
- The environmental analysis process is not a static process. It is a dynamic process which may change from one business to another.
- SWOT analysis refers to the analysis of both internal and external environments of an organisation. In this term, S stands for Strengths and W stands for Weaknesses. Both these terms are internal components of an organisation. O stands for available Opportunities of the market and T stands for possible Threats in the market. Both these are external components.
- Business risk means when an organisation is exposed to danger or threat which could lower its profits or which may hamper the achievement of target. Any threat which may harm the normal functioning of an organisation is known as business risk.

- Assessing risk means making an estimate of what level of risk is present in the given business situation. Thus, risk assessment is actually risk measurement.

2.9 Key Words □□

Environment: The surroundings around anything/ an organisation. □□

Screening: The process of evaluation or assessment of anything. □□

Scanning: The process of analysing all the parts of anything in order to develop its feature.

Monitoring: The process of keeping a constant eye on something to check on a regular basis. □□

Strengths: The ability in which someone performs very well. □□

Weakness: The inability due to which someone performs very badly. □□

Opportunity: A chance available in a given situation. □□

Threat: Threat means exposing vulnerability of something which might create an adverse impact. □□

Risk: An exposure of something to a possible loss.

2.10 Case Study: SWOT Analysis Of Apple Inc.

SWOT analysis is basically an analysis of company or organisation's strengths, weaknesses, opportunities and threats. Here is a case study of Apple Inc. on SWOT analysis.

Apple had launched its new phone iPhone 7 in an event. It has also expanded its business boundary by launching Apple watch, and Bluetooth headphones, also known as AirPod.

Apple's strengths: iPhones have created a unique brand identity for themselves. People are willingly ready to spend lakhs in the name of iPhone. The logo of Apple is a symbol of status these days. Moreover, Apple's product design is artistic, yet simple, rich and royal and creative too. Apple has customer faith and its brand value has worldwide recognition. Its brand value is so high that most of the Apple's products are often pre-ordered worldwide. Moreover, Apple utilises its image to sell a way of life of imagination, extravagance and smoothness. This is how it advertises its items: Not as a straightforward contraption, yet as a route into designed and planned world. This is why, its revenues and, subsequently, its profit margin is too high in products like Mac Laptop, iPhone, iPad, etc.

Apple's weaknesses: One of the greatest weaknesses of Apple is its high prices of products. Although its prices are high, but it restricts its buyers from upper middle class to high class. Usually, a PC can be bought for $200. On the contrary, Apple's Mac laptop costs around $1100-$1200+. If offered at a sale price, the sales reduce the price of the product by only $50-$100. Only the students are able to get the laptops at discounted prices. If we take globally, then there are a number of lower-class people who couldn't afford to buy Apple products. Apple ignores this class of customers. We can say that this is a great weakness of Apple Inc.

Apple's opportunities: Apple has witnesses a potential advantage in teaming up with various solid and existing brands identified with its commercial centre. With its new AirPods, it has collaborated with Beats earphones to present the new remote Beats X close by its iPhone 7. Moreover, Nintendo is bringing another amusement, Mario Run, to iPhone — consolidating the Apple name with the notable diversion face of Nintendo. This is another incredible brand which could get gigantic numbers from its numerous fans all over the world? Apple's present advancement can be derided, criticised or cheered. In any case, the business openings from working together with other expansive brands over the world will profit the Apple brand monstrously, insofar as it keeps on building up these business connections.

Apple's threats: Ever since Apple Inc has entered in the market, its biggest threat is innovation. It keeps on producing the same kind of products. The regular customer might lose interest after some time. While Apple's structure is smooth and short-sighted, that is actually what makes it simple to imitate. Worldwide stores sell counterfeit renditions of iPhones and iPod contacts which, outwardly, look about indistinguishable. Furthermore, numerous individuals fall for the tricks of 'overly cheap Apple items' sold on the web. Another threat to Apple products is competition. Companies like Samsung have captured the market with the launch of the concept of androids in the market. Apple has heightened its competition by not providing earphones in its new model, iPhone 7, iphone X etc. Moreover, android companies are providing the same facilities at much cheaper rates.

2.11 Self Assessment Test

1. What is environmental screening?
2. What is importance of environmental screening?
3. What is business environment analysis?
4. State different steps in business environment analysis.
5. What is SWOT analysis?
6. What is risk assessment?
7. How does the PESTLE analysis help in analysing the organizational strategies?

2.12 Answers To Check Your Progress

1. D

2. B

3. Risk

4. Strategic

2.13 Suggested/Further Readings

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Course: Business Environment	
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Concepts of Economic System

STRUCTURE

3.0 Learning Objectives

After going through this lesson, the learner should be able to:

- Know the meaning of economic system
- Know the types of economic system and differences in these economic systems
- Understand the advantages and disadvantages of different type economic systems
- Know the Indian economic system
- Understand the Govt. role in each type of economic system

3.1 Introduction

A business's success depends in part on the economic system of the country where it is located and where its sells its products/services. A nation's economic system is the combination of policies, laws, and choices made by its government to establish the systems that determine what goods and services are produced and how they are allocated. Economics is the study of how a society uses scarce resources to produce and distribute goods and services. The resources of a person, a firm, or a nation are limited. Hence, economics is the study of choices—what people, firms, or nations choose from among the available resources. Every economy is concerned with what types and amounts of goods and services should be produced, how they should be produced, and for whom. These decisions are made by the marketplace, the government, or both. In India, the government and the free-market system work together in the economy. An economic system, or economic order, is a system of production, resource allocation and distribution of goods and services within a society or a given geographic area. It includes the combination of the various institutions, agencies, entities, decision-making processes and patterns of consumption that comprise the economic structure of a given community. As such, an economic system is a type of social system. The mode of production is a related concept. All economic systems have three basic questions to ask: what to produce, how to produce and in what quantities and who receives the output of production (for whom to produce).You probably know more about economics than you realize. Every day, many news stories deal with economic matters: a union wins wage increases at General Motors, Reserve Bank of India lowers interest rates, Nifty has a record day, the president proposes a cut in income taxes, consumer spending rises as the economy grows, or retail prices are on the rise, to mention just a few examples.

3.2 Economic System: Meaning

Economic system is a social organism through which people make their living. It is constituted of all those individuals, households, farms, firms, factories, banks and government, which act and interact to produce and consume goods and services. Individuals and households put their resources (land, labour, capital and entrepreneurial skill) to one or more of their alternative uses and make their living; firms buy factors of production and organize them in the process of production, produce goods and services, and sell them to their users to make projects. Consumers are able to get the goods and services of their requirement; producers are able to produce and sell various kinds of products in appropriate quantities and so on. The system is operated by, what Adam Smith called "invisible hands", the market forces of demand and supply. An economic system is a mechanism with the help of which the government's plan and allocate accessible services, resources, and commodities across the country. Economic systems manage elements of production, combining wealth, labor, physical resources, and business people. An economic system incorporates many companies, agencies, objects, models, as well as for deciding procedures.

A modern economic system is enormously complex. Millions of people participate and contribute to its working in different capacities – as producers, traders, workers, consumers and financers and so on. Thousands of people are involved in production and distribution of single commodity. A community, before it reaches its final consumer, passes through a complex process of production and through a number of intermediary hands.

3.3 Kinds of Economic Systems

1. Free Enterprise / Market Economy

This economic system works on the principle of Laissez Faire system, i.e., the least interference by the government or any external force. The primary role of the government, if any, is to ensure free working of the economy by removing obstacles to free competition. This economic system is also known as capitalism or free market economic system. A free Enterprise Economy is characterized as follows:

- Means of production are privately owned by the people who acquire and posses them.
- Private gains are the main motivating and guiding force for carrying out economic activities.
- Both consumers and firms enjoy the freedom of choice; consumers have the freedom to consume what they want to and firms have the choice to produce what they want to.
- The factor owners enjoy the freedom of occupational choice, i.e., they are free to use their resources in any legal business or occupation;
- There exists a high degree of competition in both commodity and factor markets.
- There is least interference by the government in the economic activities of the people; the government is in fact supposed to limit its traditional functions viz, to defence, police, justice, some financial organizations and public utility services.

Advantages of a Free Enterprise/ Market Economy

- Consumers pay the highest price they want to, and businesses only produce profitable goods and services. There is a lot of incentive for entrepreneurship.
- This competition for resources leads to the most efficient use of the factors of production since businesses are very competitive.

- Businesses invest heavily in research and development. There is an incentive for constant innovation as companies compete to provide better products for consumers.

Disadvantages of a Free Enterprise/Market Economy

- Due to the fiercely competitive nature of a free market, businesses will not care for the disadvantaged like the elderly or disabled. This lack of focus on societal benefit leads to higher income inequality.
- Since the market is driven solely by self-interest, economic needs have a priority over social and human needs like providing healthcare for the poor. Consumers can also be exploited by monopolies.

2. Government Controlled Economy / Command Economy

The government-controlled economies are also called as Command, Centrally planned or Socialist economies. Such economies are, in contradistinction to the free enterprise economies, controlled, regulated and managed by the government agencies. The other features of a pure socialist economy are:

- Means of production are owned by the society or by the state in the name of the community private ownership of factors and property is abolished;
- Social welfare is the guiding factor for economic activities – private gains, motivations and initiatives are absent,
- Freedom of choice for the consumers is curbed to what society can afford for all, and
- The role of market forces and competition is eliminated by law.

Advantages of Command Economic Systems

- If executed correctly, the government can mobilize resources on a massive scale. This mobility can provide jobs for almost all of the citizens.
- The government can focus on the good of society rather than an individual. This focus could lead to more efficient use of resources.

Disadvantages of Command Economic Systems

- It is hard for central planners to provide for everyone's needs. This challenge forces the government to ration because it cannot calculate demand since it sets prices.
- There is a lack of innovation since there is no need to take any risk. Workers are also forced to pursue jobs the government deems fit.

3. Mixed Economy

A mixed economy is one in which there exist both government and private economic systems. It is supposed to combine good elements of both free enterprise and socialist economies. A mixed economy is widely known as one, which had both "public sector" (the government economy) and "private sector" (the private economy). The private sector has features of a free enterprise economy and the public sector has features of socialist economy. It is important to note here that most economies in the world today are Mixed Economies.

There are two different forms of the Mixed Economies.

Mixed Capitalist Economies

A mixed Capitalist economy is a variant of the free enterprise economic system. To this category fall the highly developed nations like the United States, U.K., France, Japan etc. though these economies have a very large government sector, their private sectors work on the principles of the free enterprise system. The government plays a significant role in preserving capitalist mode of production, ensuring a workable competition in factor and product markets, providing infrastructure for promotion of private sector economic activities.

Mixed Socialist Economies

Mixed Socialist Economies belong the countries which have adopted "socialist pattern of society: and economic planning as he means of growth and social justice (e.g. India) and the former communist countries (e.g. Russia and China) which have of late carried out drastic economic reforms and liberalized their economies for private entrepreneurship. The government of these countries takes upon themselves to control and regulate the private sector activities in accordance with the plan objectives.

Advantages of Mixed Economies

- There is less government intervention than a command economy. This results in private businesses that can run more efficiently and cut costs down than a government entity might.
- The government can intervene to correct market failures. For example, most governments will come in and break up large companies if they abuse monopoly power. Another example could be the taxation of harmful products like cigarettes to reduce a negative externality of consumption.
- Governments can create safety net programs like healthcare or social security.
- In a mixed economy, governments can use taxation policies to redistribute income and reduce inequality.

Disadvantages of Mixed Economies

- There are criticisms from both sides arguing that sometimes there is too much government intervention, and sometimes there isn't enough.
- A common problem is that the state run industries are often subsidized by the government and run into large debts because they are uncompetitive.

3.4 Difference between Capitalist, Socialist and Mixed Economy

Basis	**Capitalist Economy**	**Socialist Economy**	**Mixed Economy**
Ownership of Property	Private ownership	Public ownership	Both public and private ownership

Price Determination	Prices are determined by the market forces of demand and supply	Prices are determined by the central planning authority.	Prices are determined by central planning authority and demand and supply.
Motive of Production	Profit motive	Social welfare	The profit motive in the private sector and welfare motive in the public sector.
Role of Government	No role	Complete role	Full role in the public sector and limited role in the private sector
Competition	Exists	No competition	Exist only in the private sector
Distribution of income	Very Unequal	Quite Equal	Considerable inequalities exist.

3.5 Basic Problems Of An Economy And The Role Of Government

Whatever the nature of the economic system, all types of economies have certain common basic problems. The major economic problems faced by an economy may be classified into two broad groups: (i) micro-economic problems called basic problems, which are related to the working of the constituents of the economic system; and (ii) macro-economic problems related to the growth, stability, and management of the economy as a whole.

The way the basic problems of an economy are solved depends on the nature of the economy. While in a socialist economy, problems are solved by the government agencies, like central planning authority, in a free enterprise or mixed capitalist economy this task is performed by the Price Mechanism or Market Mechanism. Though free enterprise system is capable of bringing economic growth, it does not ensure a stable, sustained, and balanced growth. It becomes therefore inevitable for the government to intervene fair competition, and help the economy in achieving its goals – efficiency, stability, growth and economic justice.

Now, the question arises as to what should be the appropriate role of the government in economic management of the country or what should be the form, nature and extent of government's interference with market mechanism. Nevertheless, the economic role of the government can be broadly categorized on the basis of the three economic systems which presently prevail in the world, viz., Capitalist System or Free Enterprise System, Socialist System, and the Mixed-Economy System.

- **Capital Society**: In this system, the primary role of the government are: (i) to preserve and promote free market mechanism wherever it is possible to ensure a workable competition, (ii) to remove all unnecessary restrictions on the free operation of competitive market, and (iii) to provide playground and rules of the market game through necessary interventions and controls so that free competition can work effectively. It may be inferred that the government's role in a capitalist society is supposed to be limited to (a) restoration and promotion of necessary conditions for efficient working of free market mechanism; and (b) to enter those areas of production and distribution in which private entrepreneurship is lacking or is inefficient.
- **Socialist Economy**: In contract with the capitalist system, the role of government in a Socialist economy is much more exhaustive. While in the former, the government is supposed to play a limited role in the economic sphere, in the latter, it exercises comprehensive control on almost all economic

activities. In the socialist system, not only there is a complete disregard for free enterprise and market mechanism but also these systems are abolished by law. The private ownership of factors of production is replaced by the State ownership. All economic activities are centrally planned, controlled and regulated by the State. All decisions regarding production resources, allocation, employment, pricing etc., are centralized in the hands of government or the Central Planning Authority.

- **Mixed Economy**: In this system, a major part of the economy, the private sector, is allowed to function on the principles of free enterprise system or free market mechanism within a broad political and economic policy framework. The other part of the economy, the public sector, is organized and managed along the socialist pattern. The public sector is created by reserving certain industries, trade, services, and activities for the government control and management. The government prevents by an ordinance the entry of private capital into the industries reserved for the public sector. Another way of creating or expanding the public sector is nationalization of existing industries. The promotion, control and management of the public sector industries are the sole responsibility of the State. Apart from controlling and managing the public sector industries the government controls and regulates the private sector through its industrial, monetary and fiscal policies. If necessary, direct controls are also imposed.

3.6 Indian Economic System

The economy in India today resembles a capitalist economy with certain modifications. Most economies in the world exists somewhere between a market economy and a centrally planned economy – India is one of these countries that has a mixed economy with several characteristics of a market economy. India tries to change the structure of the capitalist economy to make it more appropriate for model economy situations.

As mentioned previously, India is a combination of a Socialist and a Capitalist economy. This economic system was adopted after independence with the intention of procuring the advantages of both systems while avoiding the disadvantages. The productive activities in India are divided between the government (public sector) and the people (private sector). Some examples of industries which are placed in the public sector include: the basic industries, the capital goods industries and the heavy industries whereas light industries and consumer goods industries are placed in the private sector. While the activities of the public sector are guided by welfare, the activities of the private sector are guided by profit. This creates balance in the economy as it ensures the acquisition of profit with a high level of public welfare. The public sectors are completely directed by the government whereas the private sectors are indirectly controlled by the government.

In a mixed economy, or a modified free enterprise system, private property is owned by individuals, corporations or the government. The government sets regulations which affect private property. Additionally, the government owns schools, parks, and real estate. In India, almost the entire agricultural sector is under private ownership. However, in the non-agricultural sector, three quarters of the industries are also in the private sector. Wholesale and retail trade is part of the private sector as well as air transportation which is rapidly being privatized.

The role of the public sector is supportive, so the public sector is expected to build the infrastructure which is used by the private sector. The public sector also develops the basic and capital goods industries. Their products are used by the private sector but even in this field also fast moving towards privatization. The state intervenes in any productive activity with the intention of making it more community friendly. If it is found that the private sector is cornering the stocks of a commodity and exploiting the consumers, the state setup its own units to produce the commodity and augment its supply. The public sector mainly specialized in the production of public utilities such as local transport, supply of cooking gas, supply of water and such other commodities which enter into the common budget. The government also undertakes purchase and sale of necessaries of life so as to protect the vulnerable sections of the community against an excessive rise in prices.

To conclude, a mixed economy is crucial for a developing economy like India in its initial stages. But as the economy develops the private sector rise into prominence and the mixed economy is knowingly (or unknowingly) transformed in to a market regulated economy.

3.7 Check Your Progress

Q.1. What are the central problems of an economy?

a. What to produce?

b. How to produce?

C. For whom to produce?

d. All of the above

Q.2. Which economic system is based on public ownership of property and social welfare?

a. Socialist economy

b. Capitalist economy

c. Mixed economy

d. None of the above

Q.3. Mixed economy operates with motive of __________________

a. Profit.

b. Social Welfare

c. Both (a) and (b)

d. None of the above

Q.4. In __________ type of economy there is no intervention of government.

a. Socialist economy

b. Capitalist economy

c. Mixed economy

d. None of the above

Q.5. In __________ type of economy there is no competition level.

a. Socialist economy

b. Capitalist economy

c. Mixed economy

d. None of the above

3.8 Summary

An economic system is a set of principles on which an economy can run and make decisions about the central problems it faces in the form of scarcity of resources and unlimited wants. The way scarce resources get distributed within an economy determines the type of economic system. There are three different types of Economic Systems; a market economy, a command economy, and a mixed economy. Each type of economy has its own strengths and weaknesses but all economic systems have three basic questions to ask: what to produce, how to produce and in what quantities and who receives the output of production (for whom to produce). Economic systems are grouped into command, market, and mixed systems. A centralized authority influences command systems, while a market system is under the control of forces of demand and supply. Lastly, mixed economies are a combination of command and market systems.

3.9 Keywords

Economic System: An economic system is a mechanism with the help of which the government's plan and allocate accessible services, resources, and commodities across the country.

Free Enterprise Economy: The least interference by the government or any external force.

Government Controlled Economy: Controlled regulated and managed by the government agencies.

Mixed Economy: Combination of free enterprise economy and govt. controlled economy system.

Indian Economic System: India has adopted Mixed economy system.

3.10 Self-Assessment Test

1. What is an economic system? What are the basic problems of an economic system?

2. What are the features of a mixed economic system?

3. "The fundamental economic problem of an economy is the problem of choice". Discuss.

4. Explain the role of government in solving problems arised out of different economic systems.

3.11 Answer To Check Your Progress

1. (d), 2. (a), 3. (c), 4. (b), 5. (a)

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Course: Business Environment	
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New Industrial Policy-1991 And Recent Financial And Economic Reforms In India

STRUCTURE

4.0 Learning Objectives

4.1 Introduction

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4.15 Summary

4.0 Learning Objectives

After going through this lesson, the learners will be able to:

- Know the meaning and objectives of New Industrial policy
- Understand the Financial and Economic Reforms
- Know the Need of These Reforms
- Understand the Positive and Negative Impact of New Industrial Policy

4.1 Introduction

The Indian Economy was facing a problem of illiteracy, poverty, low per capita income, unemployment and industrial backwardness etc. at the time of independence. After attaining independence in 1947 an effort was made to begin the era of planned industrial development. It causes rules, regulations and policies adopted by the government for industries. The industrial policy has injected a substantial measure of competitive environment and market thrust to industry. Many areas earlier reserved for the public sector are now open to private sector participation. The restrictions on the expansion of large industrial houses have been removed. Licensing requirements for industries have been abolished except for a strategic and defence industries. Before going into the details of regulation of Indian Industries, let us have a look at the successive industrial policies adopted by the government. After independence in 1947, India first industrial policy came into existence in the year 1948 after that next industrial policy resolution was adopted in India on 1956, next in 1973 after that in 1977, 1980, 1990 and new industrial policy 1991. We will focus on new industrial policy 1991.

4.2 Industrial Policy 1991

The overall objectives of industrial policy in India have been periodically articulated in the Industrial Policy resolution of 1948, 1956 and 1973, the industrial policy statement of 1980 and 1990. On July 24, 1991 the government announced a new industrial policy in parliament. Congress Government then, the Prime Minister of India P.V Narsimhan Rao announced new industrial policy in July, 1991 and this policy has changed the economy to large extent. In order to attune Industrial policy with the liberalized back-up to the service sector, as also to the approvals for FDI and NRI investment. The proposed legislation would also replace the Industries (Development and Regulation) Act, 1951. Since the focus has shifted from state-regulated planned development to the market-driven economy, it has been felt that industrial policy should go in tandem with liberalization. Till July 1991, the emphasis was on "regulation" The New Industrial Policy of 1991 shifts emphasis from "regulation to development". Now, the government endeavors to spread industrialization in backward areas not by directly setting up units in the public sector, but by appropriate incentives and infrastructure development initiatives to facilitate flow of private investment to backward areas.

4.3 Objectives Of New Industrial Policy

- Unshackle the Indian economy from cobweb of bureaucratic control
- Liberalizing the policy regarding FDI.
- To abolish restriction on FDI.
- Redefining the role of public sector.
- Bringing of welfare scheme of Indian industries.
- Remove restriction imposed by FERA on international trade.
- To ensure quality standards.
- Emphasis on research and development capabilities.
- Abolishing of MRTP act.
- Improve the productivity of Indian industry.

- To prepare Indian industry for globally competitive.
- Integration of Indian industry with the world.

4.4 Need Of New Industrial Policy Or Financial And Economic Reforms

1. Increase in fiscal deficit: Prior to 1991, fiscal deficit of the government had been mounting year after year on account of continuous increase in its non-development expenditure. Fiscal deficit means difference between the total expenditure and total receipts minus loans. It is equivalent to total borrowings by the government. In 1981-82, it was 5.4 per cent of gross domestic product (GDP). In 1990-91, it rose to 8.4 per cent of GDP. With a view to meeting fiscal deficit, the government is obliged to raise loans and pay interest thereon. Thus, due to persistent rise in fiscal deficit there was a corresponding rise in public debt and interest payment liability. In 1980-81, interest payment on public debt amounted to 10 per cent of total government expenditure. In 1991, amount of interest liability rose further to 36.4 percent of total government expenditure. There was serious apprehension that the government was fast heading for debt trap.

2. Increase in adverse balance of payments: Balance of payment is the difference between total exports and total imports of a country. When total imports exceed total exports, the balance of payments becomes adverse. Government granted diverse kinds of incentives and concessions to the exporters under export promotion program, yet the export did not rise to the desired extent. It was mainly due to the fact that in international market our exports could not complete in price and quality. All this was the direct result of the policy of protection so liberally pursued by the government and for so long. As against slow growth of exports there was rapid increase in imports. As a result, balance of payments deficit increased very much. Deficit of balance of payments had been rising continuously since 1980-81. For instance, in 1980-81, balance of payments on current account was adverse to the tune of Rs. 2,214 crore and it rose in 1990-91 toRs.17367crore. To meet this deficit large amount of foreign loans had to be obtained.

3. Gulf Crisis: On account of Iraq war in1990-91, prices of petrol shot up. India used to receive huge amount of remittances from Gulf countries in foreign exchange all that stopped totally. Gulf crisis thus further accentuated already adverse balance of payments position. This has increased balance of payments deficit very much.

4. Fall in foreign exchange reserves: in 1990-91India's foreign exchange reserves fell to such a low level that the same were not enough to pay for an import bill for even 10 days. Foreign exchange reserves that were Rs. 8151 crore in 1986-87 declined sharply to Rs. 6252 crore in 1989-90. The situation grew so acute that Chandrashekhar government had to mortgage country's gold to discharge its foreign debt servicing obligation.

5. Rise in prices: In India prices continued to rise very high. Average annual rate of inflation increased from 6.7 per cent to 16.7 per cent. Main reason for inflation or annual rate of increase in prices was rapid increase in the supply of money. This, in turn, was due to excessive resort to deficit financing by the government. Deficit financing implies borrowing from Reserve Bank of India by the government to meet its deficit. Bank offered this loan by printing new currency notes. Cost of production takes an upward jump due to high rate of inflation. It adversely affects domestic and foreign demand for our products.

6. Poor performance of Public Sector Undertakings (PSU): In 1951 there were just 5 enterprises in public sector in India but in 2001 their number rose 232. Several thousand crores of public funds were invested therein. In the initial 15 years their functioning was quite satisfactory but thereafter most of these suffered losses. Because of their poor performance, Public sector undertakings degenerated into liability. On account of the above compelling factors, it became inevitable for the government to adopt New Economic Policy. It was all the more necessary to increase industrial output and attract foreign capital.

4.5 Major Initiatives Of New Industrial Policy

Major initiatives or we can say features of new industrial policy are as following:

(I) Abolishing industrial licensing: For liberalize the economy, need was felt to abolishing of industrial licence except 18 industries that require Compulsory Licensing. There 18 industries were:

1. Coal and Lignite
2. Petroleum
3. Sugar
4. Animals fats and oil
5. Cigars and Cigarettes of tobacco and manufactured tobacco substitutes
6. Motor cars
7. Paper& Newsprint
8. Defence equipment
9. Hazardous chemicals
10. Drugs & Pharmaceuticals
11. Entertainment Electronics (VCR, DVD, Tape recorders)
12. White goods (Domestic Refrigerator, Dishwashing Machines Etc)
13. Tanned or Dressed Fur skins
14. Asbestos and its based products
15. Distillation and brewing of Alcoholic drinks
16. Raw hides & skin, Leather
17. Industrial explosives
18. Plywood and others wood based products and

With the passage of time this has been reduced to 14, then to 9 and later to 8 and 5 and at present only 4 industries require compulsory licensing are as follows:

1. Cigars and Cigarettes of tobacco and manufactured tobacco substitutes

2. Hazardous chemicals, Drugs and Pharmaceuticals

3. Electronics aerospace and Defence equipment

4. Industrial explosives – including detonating fuses, safety fuses, gunpowder, nitrocellulose and matches.

(2) Role of public sector: Inspite of huge investment public sector was not performing good, so need was felt to redefine the role of public sector. The number of industries reserved for public sector reduced from 17 to 8 and then further to 6.and then 6 to 3, and at present only two sectors are reserved for public sector: 1.Atomic Energy, 2.Railway operations, other than construction, operation and some maintenance functions.

(3) Foreign investment: Earlier it was necessary for every industry to take the prior approval of government which led to unnecessary delay and sometime due to frustration foreign investors do not invest to promote export of Indian goods in the world market unconditional approval was given under new industrial policy 1981 for FDI up to 51 % in high priority industries.

(4) MRTP Act: New industrial policy 1991 removed the threshold limit of assets in respect of MRTP companies this eliminates the company for prior approval of central government for expansion, establishment of new industries undertaking ,merger etc.

(5) Foreign technology: (i) Automatic permission for foreign technology agreement in high priorities industries up to 1 crore 5% royalty for domestic sales 8% for export (ii) No permission for hiring of foreign technicians

(6) Convertibility of Rupee: The new industrial Policy of the year 1991 has given the privileges to the industrial regarding import of raw material and technology. The new policy has introduced the rupee convertibility on current account as well as on capital account. The government made the current account fully convertible, while under the capital account the repayment of loan and deprecation of assets has been made convertible. Further, under the previous provisions the financial institution extending loans to industrial houses had an option to convert their 20% loans into equity it was a major threat to the industrialist in posting threat to their positions. Under the new industrial policy such as compulsory clause of conversion of loans in to equity has also been abolished.

(7) Reservation for small scale industries: In the year 2006, small scale units were defined as a unit having investment of 5 cr. in Plant and machinery. In Oct 2008, 21 items were reserved for manufacturing in small scale industries.

(8) Encouragement to industries in backward areas: Government has taken various measures to encourage the industries in backward areas. Various incentives will be offered by govt to industries in the backward region for reducing regional disparities.

(9) Freedom from administrative control: Expansion programmes launched by government are exempted from administrative controls and already existing units will be free to produce any commodity on the basis of the licensed already issued.

4.6 Appraisal Of New Industrial Policy

Positive aspect of New Industry Policy

1. Building competitiveness in Indian industries: The new industrial policy undoubtedly claims the credit of creating and promoting competitive economic conditions in the Economy. It includes:

- New Industrial policy almost removed all kinds of protections given to the domestic industry.
- It has opened the industries for private investment that were previously reserved for investment by the public sector only.
- The new industrial policy has also liberalized the location norm and has also made the import of technology free from government restrictions.
- The procedural delays have been removed leading reduced cost of the project.

2. Attracting FDI: Under the new policy the government has broken up the natural monopoly of the public sector units by attracting the private and foreign capital in to the industries that were earlier reserved for public sector. Now, in high priority industries no prior approval of the government is required for FDI Upto 51%.

3. Import of technology in India: The process of import of technology in India was simplified with grant of automatic permission in high priority industries to remove unnecessary delays that were hampering the decision making process regarding import of technology.

4. Development of global quality standard in India: The objective of new industrial policy was to focus on development of global quality standard in India for improving the quality of production in all respects. In order to promote exports and bring global competitiveness in Indian Industry. The policy emphasized the shifting of quality standard from Indian Standard Industries and International Standard Organisation.

5. Removal of MRTP act: Removal of restrictive conditions of MRTP Act like pre entry scrutiny of investment decision by MRTP commission, prior approval of centre for expansion, establishment of new undertaking. Merger, amalgamations, takeover and provisions to appoint foreign Director will strength such units.

6. Removal of restrictive condition of FERA: The Industrial policy has abolished almost all the restrictive provisions of FERA. The abolition of FERA was a major relief provided to the industries engaged in export activities.

7. Development of consumerism in India: The new Industrial Policy has shifted the role of state from regulatory in nature to managerial one. Under the new Industrial policy the state has to create competitive economic conditions to make the industry more accountable to the society. **Negative aspect of New Industry Policy:**

1**. More weight age to foreign investor:** The New Industrial Policy has laid more emphasis on FDI in India. In fact, FDI considered a panacea of all the socio-economic problem of the country. It has been decided to provide approval for direct foreign investment up to 51% foreign equity in high priority industries. H.K. Para jape agreed that 34 high priority industries, having provisions for automatic permission for foreign investment, would make it possible for large multinational companies to dominate certain growing areas of our country argued that if the same amount of incentives and concessions are being provided to indigenous industry houses then better results can be expected without taking the risk of foreign capital.

2 Exploitation of domestic resources: The natural resources are limited. Each country of the world, either developing or developed, intends to make optimum use of available resources for the overall growth and development of the country. The critics of New Industrial policy are of the opinion that the provisions of huge foreign capital in the country will lead to wastage and even misuse of resources available with the country. The multinational companies have huge marketing and financial resources. They have the latest technologies and huge production capacities. The MNCs will utilize their natural resources to produce the products belonging to non-priority categories for serving the world market. It leads to the early depletion of available resources of the country.

3. Threat to environment: the environmental laws in all the developed countries of the world are very strict and their violation leads to harsh consequences for the industries. On the other side, the environment laws in developing and least developed countries and their implementations also ineffective. Further the developing countries are victims of corruption, favouritism and other malpractices.

4. Reduction in growth of production of industrial goods: The most negative indicator goes against the industrial policy is the sudden fall in production of industrial growth. In the initial years of liberalisation the growth of industrial goods has shown the negative figures.

4.7 Suggestions For Effectiveness Of Industrial Policy

1. Effectiveness of private sector: There is a need that government should provide sufficient resources to the private sector in the form of technical support, infrastructural support, and liberal credit policy so that they can develop their industries in a good manner and can compete with the foreign enterprises.

2. Enhance the profitability of public sector: This is very important that public sector should be more efficient and profitable. The following steps should be taken:

- More and more efficient human resources are appointed.
- Promotion to employees should be on the basis of merit not on seniority basis.
- Inspections should be done properly.
- Production capacity of older public sector enterprises should be increased.
- Accounting records are properly checked with time to time.
- Non planned expenditure should be reduced at most.

3. Development of infrastructure: Government should take effective measures to strengthen the infrastructure of the economy, in the field of transportation, communication, power supply etc. In the lack of strong infrastructure, the economy of India cannot develop in the proper way.

4. Not too much dependence upon the foreign investment: The government should ensure that there is not having too much independence upon the foreign capital inflow in the country. Too much flow of foreign inflows results the deficit finance in the country resultant into negative balance of payments.

5. Proper attention to sector enterprises: Small scale sector of India needs so much improvements .Various fiscal and non –fiscal incentives should be given to small scale units to support them. If proper attention to be given to this sector, unemployment situation of the country can be reduced to greater extent because of highly labour intensive utilisation.

6. Set up units in backwards areas: To remove the regional imbalances there should be a proper set up of units in the backward areas. For this special assistance should be provided by the government to reduce the regional imbalance in the country.

7**. Support to domestic industrial units for their expansion:** Government should provide financial assistance to domestic sector unit's so that they can expand their business not only to the domestic territory but also can expand business in foreign countries also. After industrial policy 1991, National Manufacturing Policy and MSME policy was introduce to boost the manufacturing sector of India. Main points regarding these policies are as following:

4.8 National Manufacturing Policy, 2011

The success of India's economic story has mainly been due to service's sector growth. Despite strong policy measures, the industrial sector (especially manufacturing) has stagnated. The maximum contribution of the sector in the overall GDP is close to 15%, which is far less than that of other emerging economies like China (whose share is close to 45%). As a result of which, India has failed to provide gainful employment to its massive labour force. Lack of employment in the manufacturing sector has put excessive pressure on the agriculture sector to provide employment, which is not possible under any economic model. The result of this is the phenomenon called "Jobless Growth", which is specific to India.

The Government recognizing this fact and in order to promote manufacturing sector launched National Manufacturing Policy on November 2011.

4.9 Objectives Of The New Manufacturing Policy (NMP):

- Increase manufacturing growth to 14 -15 percent in the medium term.
- Increase share of manufacturing in the GDP to 25 percent by 2022.
- Create 100 million additional jobs in the manufacturing sector by 2022.
- Skill development of the rural population and urban poor so that they can be absorbed in the manufacturing sector.
- Increase domestic value addition and technological advancement in the manufacturing sector.
- Increase global competitiveness of Indian manufacturing firm.

4.10 Government Policy Support Under NMP

- The manufacturing policy proposes to create an enabling environment for the growth of manufacturing in India.
- The NMP envisages simplification of business regulations significantly.
- The NMP proposes the development of the MSMEs sector. The proposal includes technological up gradations of the MSMEs; adoption of business-friendly policies; equity investments.
- Skill Development of the youth is the most important part of the NMP.
- Setting up of National Investment and Manufacturing Zones (NIMZ) with significant incentives like easy land acquisitions, integrated industrial township development, world-class physical infrastructure.
- A total of 12 NMIZ have been announced so far by the government. Out of the total 12, 8 NIMZ are located in the Delhi-Mumbai Industrial Corridor. Other 4 NMIZ is planned to build in; Nagpur; Tumkur (Karnataka); Chittoor (Andhra Pradesh); Medak (Andhra Pradesh).

4.11 The Micro, Small and Medium Enterprises Development Act, 2006

The Micro, Small and Medium Enterprises Development Act, 2006 aims at facilitating the promotion, development and enhancing the competitiveness of micro, small and medium enterprises and for matters connected therewith or incidental thereto. The Act is operational from 2nd October2006.

Definition of Micro, Small & Medium Enterprises:

In accordance with the provision of Micro, Small & Medium Enterprises Development (MSMED) Act, 2006 the Micro, Small and Medium Enterprises (MSME) are classified in two categories:

a. Manufacturing Enterprises:

The enterprises engaged in the manufacture or production of goods pertaining to any industry specified in the first schedule to the industries (Development and regulation) Act, 1951). The Manufacturing Enterprise is defined in terms of investment in Plant & Machinery.

b. Service Enterprises:

The enterprises engaged in providing or rendering of services and defined in terms of investment in equipment. The limit for investment in plant and machinery / equipment for manufacturing / service enterprises, as notified, vide S.O. 1642(E) dtd.29-09-2006 are as under:	
Manufacturing Sector	**Investment in plant & machinery**
Micro Enterprises	Does not exceed 25 lakh rupees
Small Enterprises	More than 25 lakh rupees but does not exceed 5 crore rupees
Medium Enterprises	More than 5 crore rupees but does not exceed 10crore rupees
Service Sector	
Enterprises	**Investment in equipments**
Micro Enterprises	Does not exceed 10 lakh rupees:
Small Enterprises	More than 10 lakh rupees but does not exceed 2 crore rupees
Medium Enterprises	More than 2 crore rupees but does not exceed 5 core rupees

4.12 Aim And Object Of The Act:

The Act aims at facilitating the promotion and development and enhancing the competitiveness of small and medium scale enterprises and seeks to:

- Provide for statutory definitions of "small enterprise" and "medium enterprise".
- Provide for the establishment of a National Small and Medium Enterprises Board, a high level forum consisting of stake holders for participative review of and making recommendations on the polices.

Revised Classification applicable w.e.f. 1st July 2020			
Composite Criteria: Investment in Plant & Machinery/equipment and Annual Turnover			
Classification	Micro	Small	Medium
Manufacturing Enterprises and Enterprises rendering Services	Investment in Plant and Machinery or Equipment: Not more than Rs.1 crore and Annual Turnover ; not more than Rs. 5 crore	Investment in Plant and Machinery or Equipment: Not more than Rs.10 crore and Annual Turnover ; not more than Rs. 50 crore	Investment in Plant and Machinery or Equipment: Not more than Rs.50 crore and Annual Turnover ; not more than Rs. 250 crore

4.13 Major Financial And Economic Reforms In India

Meaning of economic reforms

Economic reforms or new economic policy refers to various policy measures and changes introduced since 1991. The common objective of all these measures is to improve productivity and efficiency of the economy by creating a more competitive environment therein.

The reforms can be classified into two broad categories:

- Liberalization, privatization and globalization measures.
- Macroeconomic reforms and structural adjustments.

Changes in the sphere of industrial licensing policy and foreign trade as well as foreign investment policies belong to the first category. Reforms touching the macro economy and economic institutions plus structural adjustments covering areas like subsidies, price environment and public sector, belong to the second category. All these initiatives are collectively referred to as the New Economic Policies (NEP).

Main features of economic reforms or New Economic Policy

1. Liberalization: Liberalization of the economy means to free it from direct or physical controls imposed by the government. Prior to 1991, government had imposed several types of controls on Indian economy, e.g., industrial licensing system; price control or financial control on goods, import license, foreign exchange control, restrictions on investment by big business houses, etc. these had dampened the enthusiasm of the entrepreneurs to establish new industries. These controls had given rise to corruption, undue delays and inefficiency. Economic reforms therefore made a bid to reduce restrictions imposed on the economy. Economic reforms were based on the assumption that market forces could guide the economy in a more effective manner than government control.

Measures Taken for Liberalization

Following measures have been taken under economic reforms for liberalisation of Indian economy:

Abolition of Industrial Licensing and Registration: The New Industrial Policy (NIP) is the first part of the liberalisation measures. Under the NIP, industrial licensing has been greatly liberalised. All industries, except a few specified ones, have been de-licensed under the NIP and liberated from the clutches of control in a bid to eliminate the obstacles to industrial growth. De-licensing of passenger car industry, bulk drugs industry, consumer electronics industry, etc. became landmarks and several new players entered these industries. Industries for which licenses are still necessary are: Liquor, b) Cigarette, c) Defence equipment's, d) Industrial Explosives, e) Dangerous Chemicals, f) Drugs. Small Scale Industry (SSI) dereservation, however, has not made much progress.

Concession from Monopolies Act: according to the provisions of Monopolies and Restrictive Trade Practices Act (MRTP Act) all those companies having assets worth more than 100 crore used to be declared MRTP firms and were subjected to several restrictions. Now the concept of MRTP has been done away with. These firms are now no longer required to obtain prior approval of the government, at the time of taking investment decisions.

Freedom for Expansion and Production to Industries: as a result of liberalisation policy, industries have been given the following freedom:

a) Prior to liberalisation under the provisions of old policy at the time of granting license government used to fix maximum limit of production capacity. No industry could produce beyond this limit. Now this limit has been removed.

b) Producers are now free to produce anything on the basis of demand in the market. Previously, only those goods could be produced which were mentioned in the licence.

Increase in the Investment Limit of the Small Industries: Investment limit of the small industries has been raised to Rs. 1 crore so as to enable them to introduce modernization. Investment limit of tiny industries has also been increased to Rs. 25 lakh.

Freedom to import Capital Goods: under the policy of liberalisation. Indian industries will be free to buy machines and raw materials from abroad in order to expand and modernise themselves.

2. Privatisation

In the context of economic reforms, privatisation means allowing the private sector to set up more and more of such industries as were previously reserved for public sector. Under it, existing enterprise of the public sector are either wholly or partially sold to private sector.

Measures adopted for Privatisation

Following measures were adopted in respect of privatisation under economic reforms:

Contraction of Public Sector: Initially in the economic development of India, public sector was accorded prime importance. As observed by Dr. Manmohan Singh, priority was given to public sector in the hope that it would help capital accumulation, industrialisation, development and removal of poverty. But none of these objectives could be realised. Policy of contraction of public sector was therefore adopted under the new economic reforms. Number of industries exclusively reserved for public sector was sector was reduced from 17 to 4. Government has been divesting its stake in public sector undertakings in the light of the redefinition of its role from being a provider of goods and services to that of a policy-maker and facilitator. Between 1991-2002 the Government has privatized assets worth US$ 6.3 billion.

2. Delicensing for Industries

3. Abolishing of MRTP Act

3. Globalisation:

Globalisation means integrating the economy of a country with the economies of other countries under conditions of freer flow of trade and capital and movement of persons across borders. “Globalisation may be defined as a process associated with increasing openness, growing economic interdependence and deepening economic integration in the world economy."

Main components of globalization of Indian economy are as under:

1. Increase in foreign investment: under economic reforms, limit of foreign capital investment has been raised from 40 per cent to 51 per cent. In 47 high priority industries foreign direct investment to the extent of 51 per cent will be allowed without any restriction and redtapism. Export trading houses will also be allowed foreign capital investment up to 51 per cent. In this regard Foreign Exchange Management act (FEMA) will be enforced.

2. Devaluation: in order to promote exports under the policy of globalisation, Indian rupee was devalued. In July 1991, rupee was devalued to the extent of 20 per cent on an average. The objective was export promotion, import substitution and attraction of foreign capital.

3. Reduction in tariffs: in order to render Indian economy beneficial internationally, custom duties and tariff imposed on imports and exports are being reduced gradually.

4. Export promotion: several measures have been taken to meet the deficit of balance of payments. Exports have been promoted. Special facilities like abolition of export duties, cheaper export credit and cuts in import duty have been provided to the exports in order to increase the share of Indian exports in world trade. The government also enhanced the duty drawback in respect of a large number of items. The greater flow of bank finance to the export sector at concessional rate also enhanced the competitiveness of exports.

5. Rupee made convertible: the government brought in partial convertibility of the rupee in 1992-93 and full convertibility on the trade account in 1993-94. The move supported the intention to give exchange rate mechanism its due role in regulating the trade flow. It also served to encourage exports.

Macroeconomic reforms and structural adjustments

The government brought about a series of macroeconomic corrections, reforms of economic institutions and structural adjustments. These included the followings:

- Fiscal reforms
- Banking Reforms
- Capital market reforms
- Containment of inflation and public debt
- Phasing out of subsidies, dismantling of price controls and introduction of market-driven price environment.
- Public sector restructuring
- Exit policy

Fiscal reforms

The fiscal reforms centered on reduction of fiscal deficits. Fiscal reforms mean increasing the revenue receipts and reducing the public expenditure of the government in a manner that production and economic welfare are not adversely affected. Its main objective was to reduce fiscal deficit that stood at 8.5 percent of GDP in 1990-91, to 4 per cent. Several reforms has been to undertake to achieve this objective, e.g., control over public expenditure, increase in taxes, sale of share of public sector enterprise and increased price of public sector products.

Taxation system reforms

Taxation system was made more scientific and rational. In respect of direct tax reforms, the government by and large tried to follow the recommendations of the Chelliah Committee. The committee had suggested moderate rates, wider tax base and improved compliance. The government scaled down corporate tax as well as personal income tax rates over two to three years. In the 1997-98 budgets, the maximum income tax rate was cut to 30 per cent from 40 per cent; and then lowers to 10 per cent from 15 per cent. The direct tax revenue as a percentage of GDP increased from 2.1 per cent in 1990-91 to 2.6 per cent in 1998-99. With the direct tax reforms, mergers and acquisitions (M&As) became easier. The government had relaxed norms of carry forward and set-off of accumulated losses and depreciation. De-mergers were also made tax neutral. As regards indirect taxes reforms, the main aim was to reduce the multiplicity of duty rates and rationalize the rate structure in both excise and customs duties. There were also substantial reductions in the actual tariffs in respect of both excise and customs duties. Peak customs duty has been brought down to 20% for all products except agro and dairy products. Customs and excise duties on a number of items were reduced in January 2004. The Government is committed to reduce the tariffs further.

Banking sector reforms

The recommendations of the Narasimham Committee formed the basis of the banking sector reforms. The government carried out a phased reduction of Statutory Liquidity Ratio (SLR) and permitted a measure of freedom and flexibility to the banks in their operations. The government also went in for partial disinvestment of its equity in the nationalised banks. It also cleared the way for the setting up of a new private sector banks in the country.

Capital market reforms

Number of development has taken place in the Indian capital market with the launching of financial reforms since July 1991. In the process the capital market is being rebuilt. Some of the important developments that have taken place in the Indian market (or the reforms that have been announced by the Central Government) are as below:

1. Setting up of Securities and Exchange Board of India (SEBI) with autonomous power as a regulatory authority over various constituents of the Capital market.

2. Abolition of the office of the Controller of Capital Issues (CCI) in 1992, which means that the pricing of new issues on the capital market will not be bureaucratically dictated.
3. Launching of Over the Counter Exchange of India (OTCEI) a place permitting smaller companies to raise funds.
4. Introduction of Screen-based System: till 1994, trading on the stock market in India was based on the open outcry system. With the establishment of the National Stock Exchange in 1994, India entered the era of screen-based trading. Within a short span of time, screen-based trading has removed the open outcry system on all the stock exchanges in the country. The key features of this system are as follows:

- Buyers and sellers place their orders on the computer.
- The computer constantly tries to match mutually compatible orders on price and time priority. • The list of unmatched orders is displayed on the screen. Put differently, it is open for inspection to all traders**.**

5. Another important reform is the introduction of electronic delivery of securities facilitated by depositories. A depository is an institution, which dematerialises physical certificates and effects transfer of ownership by electronic book entries. Traditionally trades in India were settled by physical delivery. This means that the securities had to physically move from the seller to the seller's broker, from the seller's broker to buyer's broker (through the clearing house of the exchange or directly), and from the buyer's broker to the buyer. Further, the buyer had to lodge the securities with the transfer agents of the company and the process of transfer took one to three months. This led to high paperwork cost created bad paper risk. To enable the creation of depositories to facilitate dematerialised trading in India, the central government passed the Depositories act, 1996. The National Securities Depositories Limited (NSDL), India's first depository, was set up in 1996. It was followed by the Central Securities Depositories Limited (CDSL). Both the depositories, the NSDL in particular, have recorded a significant growth in their

operations. SEBI has made settlement of trades in dematerialised (popularly called demat) form compulsory for all the stock exchanges in country. This means that if you want to buy or sell shares on any exchange you have to do it only in the dematerialised form.

6. Shifting to rolling settlement was another important reform. Till recently share transactions in India were settled on the basis of a weekly account period. (On the Bombay Stock Exchange the account period was Monday to Friday and on the National Stock Exchange the settlement account period was Wednesday to Tuesday.) This meant that purchases and sales during an account period could be squared up and at the end of the account period; transactions could be settled on a net basis. For example, if you bought 100 shares of Infosys on Bombay Stock Exchange on a Monday, at Rs. 5000 a share and sold 95 shares of Infosys on at RS. 5050 on the Friday of that week, you were required to take delivery for only 5 shares by paying RS. 20250 (Purchases consideration of Rs. 500000-Sale consideration of Rs. 479750) at the end of account period. The weekly settlement system along with the badla system of carrying forward transactions from one account period to the next led to unbridled speculative activity and periodic market crisis. So, SEBI decided to introduce rolling settlement in important scrips with effect from 1st January 2002. Under a rolling system each day constitutes an account period and its trades are settled after a few days. For example, under the T+5 rolling settlement, which was introduced initially, the trades were settled after 5 days. With effect from April 1, 2002, the T+3 settlements system was introduced. At present T+2 settlement cycle exist.

Insurance sector reforms

Opening up of the insurance sector is another important element of the reforms. This came much later in the long sequence of reforms. The Malhotra Committee report on the liberlisation of the insurance sector, had earlier recommended that foreign insurance companies be allowed to operate in India preferably in Collaboration with

Indian Companies. The Insurance Regulatory and Development Authority (IRDA) Act was passed by parliament in 1999. The Act paved the way for the entry of private sector, including foreign private sector, into the insurance business, which had been a government monopoly for decades. The move broke the monopoly of the LIC IN Life insurance and that of the GIC in health and general insurance. The new Act provides statutory backing to the IRDA and seeks to entrust it with the responsibility of regulating the insurance business in the country. Under the Act, foreign equity up to26 per cent is allowed in domestic insurance companies. It stipulates a minimum paid-up capital of Rs. 100 crore each for companies in life insurance and general insurance.

4.14 Check Your Progress

1. Consider the following statements and identify the right ones.

i. The Industrial Policy of 1948 was the first industrial policy statement by the Government
ii. It gave leading role to the private sector

(A). I only

(B). ii only

(C). both

(D). none

2. In which among the following years, a new "Liberalized Industrial Policy" in India was announced for the first time?

(A) 1986

(B) 1991

(C) 1992

(D) 1993

3. Which of the following cannot be described as an achievement of the public sector in India?

(A) Strengthening infrastructure (B) introducing modern technology

(C) Over capitalization (D) none of these

4. Which of the following industries have been reserved for the public sector under July 1991 Industrial Policy?

1. Atomic energy

2. Coal and lignite

3. Mineral oils

4. Mining of diamonds

(A) 1 and 2 (B) 1 and 3

(C) 1, 2 and 3 (D) all of them

5. Industrial licensing has been abolished for all industries by the July 1991 Industrial Policy statement except for

(A) 15 industries (B) 18 industries

(C) 22 Industries (D) 25 Industries

4.15 Summary

At the time of independence, India was really backward in industrial area. After independence govt. of India make industrial policy in 1948 and gives more attention on industrialization. In present India has rapid growth in all industrial sectors and have a sound economy. India has more competitive products in international market. To make more competitive industrialization, Indian govt. changes policies time to time and make economy stronger and more sustainable. The Industrial policy of 1948, which was the first industrial policy statement of the Government of India, was changed in 1956 in a public sector dominated industrial development policy that

remained in force till 1991 with some minor modifications and amendments in 1977 and 1980. In 1991, far reaching changes were made in the 1956 industrial policy. The new Industrial Policy of July 1991 heralded the framework for industrial development at present. These industrial policies are completing their objectives which are discussing above and some other important financial and economic reforms are also taken for better economic performance.

4.16 Key Words

New Industrial policy: Industrial policy introduced in 1991 is called new Industrial policy.

Economic Reforms: Economic reforms refer to various policy measures and changes introduced since 1991.

Globalization: A process associated with increasing openness, growing economic interdependence and deepening economic integration in the world economy.

Privatization: Privatization means allowing the private sector to set up more and more of such industries as were previously reserved for public sector.

Liberalization: Liberalization of the economy means to free it from direct or physical controls imposed by the government.

4.17 Self Assessment Test

Q1. Decribe new industrial policy and its positive and negative impacts on Indian economy.

Q2. Write about liberlisation, privatisation and globalisation**.**

Q3. What is MSMED act 2006, its objective and criteria for MSME enterprises.

Q4. What is financial and economic reforms, explain recent reforms in Indian economy?

4.18 Answer To Check Your Progress

1. (A) 2. (B) 3. (C) 4. (D) 5. (B)

4.19 Suggested/Further Readings

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Course: Business Environment	
Course Code: **MBA 105**	Author: **Dr. Rajiv Kumar**
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Fiscal And Monetary Policy In India And Their Impact On Business Environment

STRUCTURE

5.0 Learning Objectives

After going through this lesson, the learners should be able to:

- Know the Fiscal policy of India and its objectives
- Understand the techniques and important terms of fiscal policy
- Know the Monetary policy of India and its objectives
- Understand the Instruments of monetary policy and its important terms

5.1 Introduction

Economic stability and economic developments are always intertwined. One of the essential prerequisite for growth of the country as well as for sustaining it in this era of highly globalised world is existence of price stability. Of course, there are chances of occurrence of fluctuations in the economy. To overcome these fluctuations there is need of monetary and fiscal policies. Monetary and fiscal policies in any country are two macroeconomic stabilization tools. However, these two policies have often been pursued in different countries in different directions. Monetary policy is often pursued to achieve the objective of low inflation to stabilize the economy from output and price shocks. On the other hand, fiscal policy is often biased towards high growth and employment even at the cost of higher inflation. For achieving an optional mix of macroeconomic objectives of growth and price stability, it is necessary that the two policies complement each other. However, the form of complementarily will vary according to the stage of development of the country's financial markets and institutions. With increasing independence of central bank in the conduct of monetary policy from fiscal dominance during the last few decades, there has been a renewed interest in the issue of monetary and fiscal policy coordination. With increasing independence of central bank in the conduct of monetary policy from fiscal dominance during the last few decades, there has been a renewed interest in the issue of monetary and fiscal policy coordination.

5.2 Fiscal Policy Of India

Fiscal policy means the use of taxation and public expenditure by the government for stabilization or growth of the economy. According to Culbarston, "By fiscal policy we refer to government actions affecting its receipts and expenditures which ordinarily as measured by the government's receipts, its surplus or deficit." The government may change undesirable variations in private consumption and investment by compensatory variations of public expenditures and taxes. An effective fiscal policy is composed of policy decisions relating to entire financial structure of the government, including tax revenue, public expenditure, loans, transfers, debt management, and budgetary deficit and so on. The policy also tries to attain a proper balance between these foresaid units so as to achieve the best possible results in term of economic goals.

5.2.0 Objectives

Before moving on the discussion on objectives of India's Fiscal Policies, firstly know that the general objectives of Fiscal Policy.

General objectives of Fiscal Policy are given below:

- To maintain and achieve full employment.
- To stabilize the price level.
- To stabilize the growth rate of the economy.
- To maintain equilibrium in the **Balance of Payments.**
- To promote the economic development of underdeveloped countries.

Fiscal policy of India always has two objectives, namely improving the growth performance of the economy and ensuring social justice to the people.

The fiscal policy is designed to achieve certain objectives as follows:

1. Development by effective mobilization of resources: The principal objective of fiscal policy is to ensure rapid economic growth and development. This objective of economic growth and development can be achieved by mobilization of financial resources. The central and state governments in India have used fiscal policy to mobilize resources.

The financial resources can be mobilized by:

1. Major three important methods:

a. **Taxation:** Through effective fiscal policies, the government aims to mobilize resources by way of direct taxes as well as indirect taxes because most important source of resource mobilization in India is taxation.

b. **Public Savings:** The resources can be mobilized through public savings by reducing government expenditure and increasing surpluses of public sector enterprises.

c. Private Savings: Through effective fiscal measures such as tax benefits, the government can raise resources from private sector and households. Resources can be mobilized through government borrowings by ways of treasury bills, issuance of government bonds, etc., loans from domestic and foreign parties and by deficit financing.

2. Reduction in inequalities of income and wealth: Fiscal policy aims at achieving equity or social justice by reducing income inequalities among different sections of the society. The direct taxes such as income tax are charged more on the rich people as compared to lower income groups. Indirect taxes are also more in the case of semi-luxury and luxury items which are mostly consumed by the upper middle class and the upper class. The government invests a significant proportion of its tax revenue in the implementation of Poverty Alleviation Programmes to improve the conditions of poor people in society.

3. Price stability and control of inflation: One of the main objectives of fiscal policy is to control inflation and stabilize price. Therefore, the government always aims to control the inflation by reducing fiscal deficits, introducing tax savings schemes, productive use of financial resources, etc.

4. Employment generation: The government is making every possible effort to increase employment in the country through effective fiscal measures. Investment in infrastructure has resulted in direct and indirect employment. Lower taxes and duties on **small-scale industrial (SSI)** units encourage more investment and consequently generate more employment. Various rural employment programmes have been undertaken by the Government of India to solve problems in rural areas. Similarly, self employment scheme is taken to provide employment to technically qualified persons in the urban areas.

5. Balanced regional development: there are various projects like building up dams on rivers, electricity, schools, roads, industrial projects etc run by the government to mitigate the regional imbalances in the country. This is done with the help of public expenditure.

6. Reducing the deficit in the Balance of Payment: some time government gives export incentives to the exporters to boost up the export from the country. In the same way import curbing measures are also adopted to check import. Hence the combine impact of these measures is improvement in the balance of payment of the country.

7. Increases national income: It's the strength of the fiscal policy that is brings out the desired results in the economy. When the government wants to increase the income of the country then it increases the direct and indirect taxes rates in the country. There are some other measures like: reduction in tax rate so that more peoples get motivated to deposit actual tax.

8. Development of infrastructure: when the government of the concerned country spends money on the projects like railways, schools, dams, electricity, roads etc to increase the welfare of the citizens, it improves the infrastructure of the country. A improved infrastructure is the key to further speed up the economic growth of the country.

9. Foreign exchange earnings: when the central government of the country gives incentives like, exemption in custom duty, concession in excise duty while producing things in the domestic markets, it motivates the foreign investors to increase the investment in the domestic country.

5.3 Techniques Of Fiscal Policy

1. **Taxation policy:** One of the important sources of revenue for government of India is the tax revenue. Both the direct and indirect taxes are being levied by the government of India. The total tax revenue collected by the government of India stands at 72.13% of the total revenue of the government. The main objectives of taxation policy in India include mobilization of resources for financing economic development and formation of capital by promoting saving and investments.
2. **Public expenditure policy:** Public expenditure is an expenditure of the government and is mostly related to the development activities, viz. development of infrastructure, health facilities, industry, and educational institutions and so on. Some important features of this policy are:
   - Development of infrastructure
   - Development of public enterprises
   - Support to private sector
   - Social welfare and employment programmes
3. **Public debt policy:** The government is taking recourse to public debt for financing its development expenditure. The total public debt of the central government includes internal and external debt.
   - The internal debt indicates the amount of loan raised by the government from within the country.
   - The external debts indicate the amount of loan raised by the government from international financing agencies.
4. **Deficit financing policy:** The deficit financing in India indicates loan taking by the government from the RBI in form of issuing fresh dose of currency. Deficit financing helps the country by providing necessary funds meeting the requirements

of economic growth but at same time, it also creates the problem of inflationary rise in prices. Thus it must be kept within the management limit.

5.4 Important Terms In Fiscal Policy

5.4.0 Revenue:

Every form of income which do not increase the financial liabilities of a government or an organization i.e., tax-income, non-tax income, grants.

5.4.1 Non-revenue:

Every form of income which increases the financial liability of a government or any organization namely borrowings of an organization.

5.4.2 Revenue Receipts:

a) Tax revenue receipts:

It includes all the money earned by the government through direct and non-direct taxes

b) Non – tax revenue receipts:

It comprises all the money received by the government through non-tax sources.

Non-tax sources:

- Interests earned by the nation through all the loans it lent
- **Profits & dividends** from the public sector undertakings
- **Grants** – **External grants** from different parts of the world to the country
- **Internal grants** from the central government to the state governments
- **Fees, fines** levied by the government
- **Earnings** from the fiscal **services** like currency printing & general services like irrigation, power distribution etc

5.4.3 Expenditure:

a) Revenue expenditure:

Revenue expenditure is a kind of consumptive expenditure that does not lead to creation of productive assets. It increases the financial liabilities or decreases the financial assets. It consists of:

- **Subsidies** given by the government in different sectors
- **Interests** paid by the government for all the loans it has taken
- **Salaries, provident fund, pensions** paid to the employees by the government
- Expenditures towards social **services** like education, health care etc & non-capital defense expenditure
- **Grants** extended by the government towards other nations and states.

b) Capital expenditure:

Capital expenditure is a kind of expenditure that increases the financial assets or decreases the financial liabilities. It consists of:

- Capital expenditure by the government on **general services** like infrastructure, railways etc.
- Capital D**efence expenditure** like purchase of weapons, defence infrastructure etc.
- **Loans** extended by the central government to the state governments, other countries etc.
- **Loans repaid** by the government which have been previously received.
- *Deficit*

5.4.4 Important Types of Deficits

a) Fiscal deficit

b) Primary deficit

c) Revenue deficit

d) Effective revenue deficit

e) Monetized deficit

a) Fiscal deficit:

Fiscal deficit reflects the extent of market borrowings by the government. The more the government borrows the lower the credit worthiness of the government, the higher the interest burden. It also means the government is spending beyond its means i.e., more than its income.

Fiscal deficit = Total expenditure – (revenue receipts + non-debt creating capital receipts)

Non-debt creating capital receipts = disinvestments from PSUs, sale of assets by the Govt. recovery of past loans

b) Primary deficit:

Primary deficit shows what government's fiscal deficit would have been if there was no burden of interest payments .A high primary deficit would mean that fiscal deficit is not on account of interest payments but due to some structural factors. A low primary deficit would mean that a large part of fiscal deficit is on account of interest payments.

Primary deficit = Fiscal deficit – interest payments

c) Revenue deficit:

If the balance of total revenue receipts and total revenue expenditures is negative, it is said to be the revenue deficit. Revenue deficit shows that the government is not able to meet its day to day expenditures.

Revenue deficit = Revenue expenditure – Revenue receipts

d) Effective Revenue deficit:

This concept is given by the former president of India **Pranab Mukarjee** in the Union budget 2012-13 in the context of amendment of Fiscal Responsibility & Budget management Act.

Effective revenue deficit = Revenue deficit – those grants given to states that are used by the states for productive purposes

e) Monetized deficit:

Monetized deficit is the deficit which is plugged by the government through **borrowing** from the **RBI**. It means financing the deficit by printing more currency notes by the RBI.

5.4.5 Merits of fiscal policy

1. Capital formation
2. Mobilization of resources
3. Incentives to savings
4. Reduction of inequality
5. Alleviation of poverty and unemployment

5.4.6 Demerits of fiscal policy

1. Instability
2. Defective tax structure
3. Negative return of the public sector
4. Inflation
5. Growing inequality

5.4.7 Suggestions for necessary reforms in fiscal policy

1. Progressive taxes
2. Checking tax evasion
3. Increasing reliance on direct taxes

4. Simplified tax structure
5. Reduction of Non-development expenditure
6. Checking blank money.

The union budget 2018-19 shows an update in the government fiscal target which was revised to 3.3% in the GDP as opposed to 3% previously. While the estimated fiscal deficit budget for fiscal year 2017-18 was 3.2 % of the GDP, now after the declaration the new budget the revised estimated target is 3.5% of the GDP. Apart from the government will also be targeting on reducing the debt to GDP ratio to 40% from the present ratio of 49.4%.

5.5 Monetary Policy Of India

Monetary policy is primarily concerned with the management of supply of money in a growing economy and managing the rate of growth of money supply per period. The Reserve Bank of India (RBI) is vested with the responsibility of conducting monetary policy. This responsibility is explicitly mandated under the Reserve Bank of India Act, 1934. The Monetary and Credit Policy is the policy statement, traditionally announced twice a year, through which the Reserve Bank of India seeks to ensure price stability for the economy. These factors include - money supply, interest rates and the inflation. In banking and economic terms money supply is referred to as M3 - which indicates the level (stock) of legal currency in the economy. Besides, the RBI also announces norms for the banking and financial sector and the institutions which are governed by it.

5.6 Main Goals Of Monetary Policy Of India

5.6.0 Maintain price stability:

The primary objective of monetary policy is to maintain price stability while keeping in mind the objective of growth. Price stability is a necessary precondition for sustainable growth. To maintain price stability, inflation needs to be controlled. The government of India sets an inflation target for every five years. RBI has an important role in the consultation process regarding inflation targeting. The current inflation targeting framework in India is flexible in nature.

5.6.1 Monetary policy framework: While the Government of India sets the Flexible Inflation Targeting Framework in India, it is the Reserve Bank of India (RBI) which operates the Monetary Policy Framework of the country.

- The amended RBI Act explicitly provides the legislative mandate to the Reserve Bank to operate the monetary policy framework of the country.
- The framework aims at setting the policy (repo) rate based on an assessment of the current and evolving macroeconomic situation, and modulation of liquidity conditions to anchor money market rates at or around the repo rate.
- Repo rate changes transmit through the money market to the entire financial system, which, in turn, influences aggregate demand – a key determinant of inflation and growth.
- Once the repo rate is announced, the operating framework designed by the Reserve Bank envisages liquidity management on a day-to-day basis through appropriate actions, which aim at anchoring the operating target – the weighted average call rate (WACR) – around the repo rate.

5.6.2 Monetary Policy Committee (MPC)

Now in India, the policy interest rate required to achieve the inflation target is decided by the Monetary Policy Committee (MPC). MPC is a six-member committee constituted by the Central Government (Section 45ZB of the amended RBI Act, 1934).The MPC is required to meet **at least four times in a year**. The quorum for the meeting of the MPC is four members. Each member of the MPC has one vote, and in the event of an equality of votes, the Governor has a second or casting vote.

The resolution adopted by the MPC is published after the conclusion of every meeting of the MPC. Once in every six months, the Reserve Bank is required to publish a document called the **Monetary Policy Report** to explain: (1) the sources of inflation and(2) the forecast of inflation for 6-18 months ahead.

5.6.3 The present Monetary Policy Committee (MPC)

The Central Government in September 2016 constituted the present MPC as under:

1. Governor of the Reserve Bank of India – Chairperson, *ex officio*;

2. Deputy Governor of the Reserve Bank of India, in charge of Monetary Policy – Member, *ex officio*;

3. One officer of the Reserve Bank of India to be nominated by the Central Board – Member, *ex officio*;

4. Shri Chetan Ghate, Professor, Indian Statistical Institute (ISI) – Member;

5. Professor Pami Dua, Director, Delhi School of Economics – Member; and

6. Dr. Ravindra H. Dholakia, Professor, Indian Institute of Management, Ahmedabad – Member.(Members referred to at 4 to 6 above, will hold office for a period of four years or until further orders, whichever is earlier.

The Reserve Bank of India defines the monetary aggregates as:

- **Reserve Money (M0)**: Currency in circulation + Bankers' deposits with the RBI + 'Other' deposits with the RBI = Net RBI credit to the Government + RBI credit to the commercial sector + RBI's claims on banks + RBI's net foreign assets + Government's currency liabilities to the public – RBI's net non-monetary liabilities. M0 outstanding was ₹14.75 trillion in August 2017.
- **M1**: Currency with the public + Deposit money of the public (Demand deposits with the banking system + 'Other' deposits with the RBI). M1 was 184 per cent of M0 in August 2017.
- **M2**: M1 + Savings deposits with Post office savings banks. M2 was 879 per cent of M0 in August 2017.
- **M3**: (Broad concept of money supply)M1+ Time deposits with the banking system = Net bank credit to the Government + Bank credit to the commercial sector + Net foreign exchange assets of the banking sector + Government's

currency liabilities to the public – Net non-monetary liabilities of the banking sector (Other than Time Deposits). M3 was 880 per cent of M0 in August 2017.

- **M4**: M3 + All deposits with post office savings banks (excluding National Savings Certificates).

5.7 Instruments/Techniques Of Monetary Policy

Broadly, instruments or techniques of monetary policy can be divided into two categories:

(A) Quantitative or General Methods.

(B) Qualitative or Selective Methods.

A. Quantitative or General Methods:

1. Bank Rate or Discount Rate:

Bank rate refers to that rate at which a central bank is ready to lend money to commercial banks or to discount bills of specified types. Thus by changing the bank rate, the credit and further money supply can be affected. In other words, rise in bank rate increases rate of interest and fall in bank rate lowers rate of interest.

During the course of inflation, monetary authority raises the bank rate to curb inflation. Higher bank rate will check the expansion of credit of commercial banks. The banks will be left with fewer resources which would restrict the credit creating capacity of the bank. On the contrary, during depression, bank rate is lowered; business community will prefer to have more and more loans to pull the economy out of depression. Therefore, bank rate or discount rate can be used in both types of situation i.e. inflation and depression.

2. Open market operations:

By open market operations, we mean the sale or purchase of securities. As it is known that the credit creating capacity of the commercial banks depend on the cash reserves of the banks. In this way, the monetary authority (Central Bank) controls the credit by affecting the base of the credit-creation by the commercial banks. If the credit is to be decreased in the country, the central bank begins to sell securities in the open market.

This will result to reduce money supply with the public as they will withdraw their money with the commercial banks to purchase the securities. The cash reserves will tend to diminish. This happens in the period of inflation. During depression when prices are falling, the central bank purchases securities resulting in expansion of credit and aggregate demand.

3. Variable Reserve Ratio:

The commercial banks have to keep given percentage as cash-reserve with the central bank. In lieu of that cash ratio, it allows commercial banks to contract or expand its credit facility. If the central bank wants to contract credit (during inflation period) it raises the cash reserve ratio. As a result, commercial banks are left with fewer amounts of deposits. Their favour to credit is curtailed. If there is depression in the economy, the reserve ratio is reduced to raise the credit creating capacity of commercial banks. Therefore, variable reserve ratio can be used to affect commercial banks to raise or reduce their credit creation capacity.

CRR is cash reserve ratio which is 4% of NDTL. It means banks have to keep aside cash and can't lend it to anyone. So basically a reserve is created for bank.

4. Change of Liquidity:

According to this method, every bank is required to keep a certain proportion of its deposits as cash with it. When the central bank wants to contract credit, it raises its liquidity ratio and vice versa. SLR(Statutory liquidity ratio) which is 21.5% of NDTL is similar as CRR just that now bank have to keep aside these many cash, gold, RBI approved securities. They are not allowed to lend this and they don’t get any interest on these as these are just kept untouched by the banks.

B. Qualitative or Selective Methods:

1. Change in Marginal Requirements

Under this method, the central bank effects a change in the marginal requirement to control and release funds. When the central bank feels that prices are rising on account of stock-piling of some commodities by the traders, then the central bank controls credit by raising the marginal requirements. (Marginal requirement is the difference between the market value of the assets and its maximum loan value). Let us suppose, a borrower pledged goods worth Rs. 1000 as security with a bank and gets a loan amounting to Rs. 800.Thus marginal requirement is Rs. 200 or 20 percent. If this margin is raised, the borrower will have to pledge goods of greater value to secure loan of a given amount. This would reduce money supply and inflation would be curtailed. Similarly, in case of depression, central bank reduces margin requirement. This will in turn raise the credit creating capacity of the commercial banks. Therefore, margin requirement is a significant tool in the hands of central authority during inflation and depression.

2. Regulation of consumer credit

During inflation, this method is followed to control excess spending of the consumers. Generally the hire purchase facilities or installment methods are used to reduce to the minimum to curb the expenditure on consumption. On the contrary, during depression period, more credit facilities are allowed so that consumer may spend more and more to pull the economy out of depression.

3. Direct Action

This method is adopted when some commercial banks do not co-operate with the central bank in controlling the credit. Thus, central bank takes direct action against the defaulter. The central bank may take direct action in a number of ways as under.

(i) It may refuse rediscount facilities to those banks that are not following its directions.

(ii) It may follow similar policy with the bank seeking accommodation in excess of its capital and reserves.

(iii) It may change rates over and above the bank rate.

(iv) Any other strict restrictions on the defaulter institution.

4. Rationing of the credit:

Under this method, the central bank fixes a limit for the credit facilities to commercial banks. Being the lender of the last resort, central bank rations the available credit among the applicants.

Generally, rationing of credit is done by the following four ways.

(i) Central bank can refuse loan to any bank.

(ii) Central bank can reduce the amount of loans given to the banks.

(iii) Central bank can fix quota of the credit.

(iv) Central bank can determine the limit of the credit granted to a particular industry or trade.

5. Moral Persuasion or Advice:

In the recent years, the central bank has used moral suasion also as a tool of credit control. Moral suasion is a general term describing a variety of informal methods used by the central bank to persuade commercial banks to behave in a particular manner. Moral suasion takes the form of Directive and Publicity.

5.8 Check Your Progress

Multiple choice questions

1.——— means the use of taxation and public expenditure by the government for stabilization or growth of the economy.

a. Monetary policy

b. Fiscal policy

c. Both a and b

d. None of the above

2. Which of the following are the techniques of fiscal policy?

a. Taxation policy

b. Public expenditure policy

c. Deficit financing policy

d. All of the above

3.———— is primarily concerned with the management of supply of money in a growing economy and managing the rate of growth of money supply per period.

a. Monetary policy

b. Fiscal policy

c. Taxation policy

d. Deficit financing policy

4. Which of following are the quantitative methods of monetary policy?

a. Bank rate

b. Variable reserve ratio

c. Open market operations

d. All of the above

5. Which of the following reflects Fiscal deficit – interest payments?

a. Fiscal deficit

b. Primary deficit

c. Revenue deficit

d. None of the above

5.9 Summary

Monetary and fiscal policies in any country are two macroeconomic stabilization tools. However, these two policies have often been pursued in different countries in different directions. Monetary policy is often pursued to achieve the objective of low inflation to stabilize the economy from output and price shocks. On the other hand, fiscal policy is often biased towards high growth and employment even at the cost of higher inflation. For achieving an optional mix of macroeconomic objectives of growth and price stability, it is necessary that the two policies complement each other. However, the form of complementarily will vary according to the stage of development of the country's financial markets and institutions. With increasing independence of central bank in the conduct of monetary policy from fiscal dominance during the last few decades, there has been a renewed interest in the issue of monetary and fiscal policy coordination. With increasing independence of central bank in the conduct of monetary policy from fiscal dominance during the last few decades, there has been a renewed interest in the issue of monetary and fiscal policy coordination. Fiscal policy means the use of taxation and public expenditure by the government for stabilization or growth of the economy. The government may change undesirable variations in private consumption and investment by compensatory variations of public expenditures and taxes. An effective fiscal policy is composed of policy decisions relating to entire financial structure of the government, including tax revenue, public expenditure, loans, transfers, debt management, and budgetary deficit and so on. The policy also tries to attain a proper balance between these foresaid units so as to achieve the best possible results in term of economic goals. Monetary policy refers to the use of **monetary instruments** under the control of the **central bank** to regulate magnitudes such as interest rates, money supply and availability of credit with a view to achieving the **ultimate objective of economic policy.** Both of the policy plays a major role in Indian economy and Government of India makes several changes in these policies for its effective implementations.

5.10 Key Words

Monetary policy, Fiscal policy, Reserve Bank of India, Bank rate, Fiscal deficit, Primary deficit, Revenue deficit

5.11 Self Assessment Test

1. What is Fiscal policy? What are its objectives?

2. Explain the techniques of Fiscal policy?

3. Define Monetary policy. What are its objectives?

4. Explain the instruments or techniques of monetary policy?

5. What are credit control measures of the RBI? Explain each in brief.

5.12 Answer To Check Your Progress

Answer of multiple choice questions:

1 b. Fiscal policy

2. d. All of the above

3. a. monetary policy

4. d. All of the above

5. b. Primary deficit

5.13 Suggested/ Further Readings

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Course: Business Environment	
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Kinds Of Business Environment And Emerging Sectors Of Indian Economy

STRUCTURE

6.0 Learning Objectives

After going through this lesson, the learner should be able to:

- Understand type of business environment.
- Distinguish between internal and external business environment.
- Understand different factors of macro business environment.
- Know the emerging sectors of Indian economy.

6.1 Introduction

Environment is sum or collection of all internal and external factors such as employees, customer's needs and expectations, supply and demand, management, clients, suppliers, owners, activities by government, innovation in technology, social trends, market trends, economic changes, etc. These factors affect the function of the company and how a company works directly or indirectly. Sum of these factors influences the companies or business organisations environment and situation. Business environment is classifies into two categories internal business environment and external business environment.

6.2 Internal Business Environment

Internal Environment: The factors of the internal business environment can best be explained by the five Ms:

- Man
- Materials
- Machines
- Management of Time
- Money

1. **Man**: Man, the first of the five Ms is the most significant factor. The right man for the right position is a guarantee for organizational effectiveness and efficiency. Thus, unpunctuality and absenteeism, alcoholism, poor training, unsafe acts, incompetence are just some of the attributes of man at work that could cost business ventures. Human resources decide the working of the other four basic business resources. People make sure materials, machines; mines and money are utilized in a productive manner in order to achieve goals or aims and objectives of organizations and enterprises. Poor employment practices are unfavourable to the sustenance of such ventures. With the right person in the right job, a large portion of effective business management can be achieved.

2**. Materials**: Without materials, human resource is useless. Good organizations know that materials needed for any business or service must be in place before 'man' can be of use in any business. Supply chain departments came out of this line of thinking and have been a very useful aspect of business management. A group of cement factory workers waiting for supply of cement may have nothing much to do as long as the supply does not arrive. Even if it arrives, but it the quality is poor, the production is affected badly. Quality compromised is business compromised. Poor quality of materials often ruins entrepreneurship.

3. **Machines**: The metal contraptions called machines have made man fulfil almost effortlessly various dreams of creating things that make existence more worthwhile. Machines have replaced man in tilling, planting and harvesting. Man has been replaced with looms in cotton and fabric processing. Countless other ventures requiring physical exertions or force have been taken over by things fixed with gears, bolts and nuts and conveyor belts. Recently, computers joined in the fray of increasing production and reduction in time spent by man for manufacturing and general production of goods and services. However, without man and materials, machines will be useless. They need to be operated by man and fed with materials which are again a doubtless fact.

4. **Management of time**: Time management is an aspect of business that has been employed by effective and successful business ventures to optimize delivery. Unpunctuality and absenteeism of man at work is a large chunk of time off production. Poor time management is as hopeless as a broken-down machine, an indisposed employee or lack of adequate materials for production of goods or services. Various schemes have been used by successful enterprises to guarantee proper and efficient use of time by man and machine, including timely delivery of materials, to ensure business sustainability. Compromising time is equal to a business venture shooting itself in the foot.

5. **Money** : Without money, no venture or enterprise can motivate employees, get quality and sufficient materials, get the proper machines and maintain them or even ascertain that time is properly managed. Money management, when not organized has been the most common factor in the collapse of enterprises in history. The quantity and quality of money expended in enterprises is directly related to the fruitfulness of the same over time. The accounts department has been revolutionized over the years, by man, to guarantee maximum operations of surviving business organizations. Where there is not enough money, good workers, materials, or machines cannot be gathered.

6.3 External Business Environment

As stated earlier, the external business environment consists of a **micro environment** and a **macro environment.**

6.3.1 Micro Environment: "The micro environment consists of the actors in the company's immediate environment that affects the performance of the company. These include the suppliers, marketing intermediaries, competitors, customers and the public’s."

- **Suppliers:** An important force, in the micro environment of a company is the suppliers, i.e., those who supply the inputs like raw materials and components to the company. The importance of reliable source/sources of supply to the smooth functioning of the business is obvious. Uncertainty regarding the supply or other supply constraints often compels companies to maintain high inventories causing cost increases.

- **Customers:** As it is often exhorted, the major task of a business is to create and sustain customers. A business exists only because, of its customers. Monitoring the customer sensitivity is, therefore, a prerequisite for the business success. A company may have different categories of consumers like individuals, households, industries and other commercial establishments, and government and other institutions. For example, the customers of a tyre company may include individual automobile' owners, automobile manufacturers, public sector transport undertakings and other transport operators. Depending on a single customer is often too risky because it may place the company in a poor bargaining position, apart from the risks of losing business consequent to the winding up of business by the customer or due to the customer's - switching over to the competitors of the company.
- **Competitors:** A firm's competitors include not only the other firms which market the same or similar products but also all those who compete for thee discretionary income of the consumers. For example, the competition for a company's televisions may come not only from other T.V manufacturers but also from two-wheelers, refrigerators, cooking ranges, stereo sets and so on and from Firms offering savings and investment schemes like banks, Unit Trust of India, companies accepting public deposits or issuing shares or debentures etc.
- **Marketing Intermediaries:** The immediate environment of a company may consist of a number of marketing intermediaries which are "firms that aid the company in promoting, selling and distributing its goods to final buyers”. The marketing intermediaries include middlemen such as agents and merchants who "help the company find customers or close sales with them", physical distribution firms which "assist the company in stocking and moving goods from their origin to their destination such as warehouses and transportation firms; marketing service agencies which "assist the company in targeting and promoting its products to the

right markets such as advertising agencies, marketing research firms, media firms and consulting firms; and financial intermediaries which finance marketing activities and insure business risks.

- **Financiers:** Another important micro environmental factor is the financiers of the company. Besides the financing capabilities, their policies and strategies, attitudes (including attitude towards risk), ability to provide non-financial assistance etc. are very important.
- **Publics:** A company may encounter certain publics in its environment. A public is any group that has an actual or potential interest in or impact on an organization's ability to achieve its interests. Media publics, citizen's action publics and local publics are some examples.

6.3.2 Macro environment

A company and the forces in its micro environment operate in a larger macro environment of forces that shape opportunities and pose threats to the company. The macro forces are, generally, more uncontrollable than the micro forces. When the macro environment is uncontrollable, the success of a company depends on its adaptability to the environment. For example, if the cost of the imported components increases substantially because of the depreciation of the domestic currency, a solution may be their domestic manufacture. Important macro environment factors include economic environment, political and regulatory environment, social/cultural environment, demographic environment, technological environment, natural environment, and global environment.

6.3.2.1 Political environment

Business units are affected by the political environment through various means. Thus, it is essential to have a stable political environment for the growth of the business. Political stability, relation with other countries, Centre-State relations, the views of the opposition parties, etc. are the major elements of the political environment. Therefore, the stability and efficiency of political environment lead to business growth. Long-term plans are difficult to formulate while there is lack of proper political environment. Also, the business is drastically affected by the unstable government. Likewise, business is also influenced by the relations of the government with other countries. Friendly relations with other countries provide a favourable environment for foreign trade. A political system, including kingship, democratic, socialist, etc., as well as political openness to the market forces is referred to as political environment of a country. Business activities in a country are widely affected by its political environment.

- A political system, including kingship, democratic, socialist, etc., as well as political openness to the market forces is referred to as the political environment of a country.
- The major elements of the political environment are Political System, Political Processes, Stability of Political Structure and Centre-State Relations.
- On the basis of the ownership and distribution of resources, the economic system can be grouped into three categories, namely capitalist economy, socialist economy and mixed economy.
- Parliament is the supreme legislative body of Indian Union which comprises of Lok Sabha and Rajya Sabha.
- Public sectors comprise the government-owned corporations in which Central or state governments hold the majority of public shares which should not be less than 51%.
- The free-market mechanism can fail due to various other reasons, therefore, in such a situation; the intervention of a government plays a significant role in the growth of an economy.
- Various reasons behind the failure of the free-market mechanism can be inequitable distribution of goods and job opportunities, the existence of perfect competition, judgement of individuals, emphasis on profit, low priority for public utilities, growth of monopolies, etc.

- There are various strategic roles of the public sector in the Indian economy, such as development of defence industries, capital formation, development of power projects, etc.

Different Economic Systems in India

Capitalist economy: A capitalist economy refers to an economy that works on the principle of the free market mechanism. It is also termed as laissez faire system. In a capitalist economy, the role of government is very limited. The main functions of government, as given by Adam Smith, are to maintain law and order in a country, make national defence stronger, and regulate the money supply. According to Smith, the market system administers various economic functions. However, over a period of time, the functions of government in an economy have increased. In a capitalist economy, the main responsibilities performed by the government are as follows:

- Developing and sustaining the free market mechanism system.
- Eliminating any kind of restrictions on the working of a free competitive market.
- Increasing the effectiveness of the free competitive market system through various measures.

Socialist economy: In a socialist economy, the function of government is entirely different from the function of government in a capitalist economy. In a capitalist economy, the government acts as a regulatory and complementary body. On the other hand, in a socialist economy, the government plays a comprehensive role in almost all economic activities, such as production, distribution, and consumption, of a nation. In a socialist economy, not only the ownership of private property is allowed to a limited amount, but the concept of the free market mechanism is also eliminated. The private ownership of resources, in a socialist economy, is changed by state ownership. In addition, in a socialist economy, the government plans and regulates all the economic activities centrally at a state level. Moreover, the decisions related to production, allocation of resources, employment, pricing, and consumption, are completely dependent on the government or its central planning authority. In a socialist economy, an individual's decisions are totally dependent on the limit decided by the government. For example, individuals are given the freedom of choice, but it is subject to the limitations of policy framework of the socialist economy.

The objective of the government in a socialist economy is the same as in the capitalist economy, such as growth, efficiency, and maintaining justice. However, the ways adopted by the socialist economy to achieve those objectives are different from the capitalist economy. For example, in the capitalist economy, the main force of motivation is the private profit, whereas, in the social economy, the encouraging factor is the social welfare. The socialist way of managing an economy facilitates the elimination of various evil activities of the capitalist economy, such as labour exploitation, unemployment, and inequality in the society.

Mixed economy:

Mixed economy refers to an economy that comprises the features of both, the socialist economy and capitalist economy. This implies that working of a mixed economy is based on the principles of the free market mechanism and centrally planned economic system. In a mixed economy, the private sector is encouraged to work on the principle of the free market mechanism under a political and economic policy outline decided by the government. On the other hand, the public sector, in a mixed economy, is involved in the growth and development of public utilities, which is based on the principle of socialist economy. In a mixed economy, the public sector comprises certain industries, businesses, and activities that are completely owned, managed, and operated by the government. Moreover, in a mixed economy, certain laws have been enacted by the government to restrict the entry of private entrepreneurs in industries reserved for the public sector. Apart from this, the government also strives hard for the expansion of the public sector by nationalising various private ventures. For example, in India, the government has nationalised several private banks, which has resulted in the expansion of the public sector. Besides working for the growth and development of the public sector, the government, in a mixed economy, controls the activities of the private sector by implementing various monetary and fiscal policies.

6.3.2.2 Economic environment

Economic environment of a country encompasses external factors which have a significant effect on the creation and dissemination of wealth. The demand and supply of a firm are directly influenced by such economic factors. From the financial point of view, it also justifies the viability of a country regarding the carrying out of business practices. The economic environment of a firm comprises various external factors like economic conditions, economic system and economic policies. A country's economic condition can be explained in the form of the income distribution, per capita income, economic nature, economic resources, and so on.

Demand is a very important element of the economic environment. The demand for products of a firm is influenced by the confidence or insecurities of consumers and their buying ability. Hence, the economic environment has a crucial role to play in the decision making of a business. The economic system acts as the basis for determining the degree of private business. There are several types of economic system followed across nations. Some nations have free market economies or capitalist economies whereas some have centrally planned economy or socialist economy. There are also some countries which follow the mixed economy, i.e., carrying characteristics of both capitalist and socialist economies.

Economic policies

For giving a boost to the development of the country and eliminating the problems of the economy (such as poverty, lack of infrastructure, low industrial production, and so forth) India embarked on the path of economic reforms in the year 1991. Economic policy enables the government to formulate and take various actions for the economy's welfare. These actions involve designing yearly budgets, framing tax rates and other plans. In a business environment, such economic policies influence the nature of ownership, labour markets, industrial relations and the other related aspects.

Both the internal and external factors influence the formulation of the economic policy of the nation. The political beliefs and philosophy of the various political parties come under the internal factors, whereas, the several international institutions such as World Bank, International Monetary Fund (IMF), credit rating agencies come under the external factors. By formulating the economic policy, a broad approach was taken to achieve a notable position in the world economy. The economic reforms of 1991 transformed the prevailing economic mind-set of India. The protectionism image was eliminated and the nation became liberal. The doors were opened to foreign investors and they were permitted to invest in Indian firms and organisations. Huge amounts of funds flowed into the Indian economy by way of FDI and portfolio investments. For enjoying the full benefits from such economic policies, some level of consistency between economic policies and the type of trade was maintained. However, while the new economic policies were formulated, the old ones were also kept in mind. This was done with the objective of keeping developmental targets in mind.

Fiscal Policy

Fiscal policy implies the policy of the government regarding expenditure and tax. It is a form of economic policy which regulates and controls the management of public debt, borrowings, expenditure and tax system within a country. The prime emphasis of fiscal policy is on the currency flow in a specific economy. The process of flow of money is initiated by the private sector which is normally transferred to the government. The government makes use of these funds for the economy's welfare. Private sector uses the tax system as a medium to channelize funds to the government and these funds then return to the economy by the way of public expenditure. Management of public debt is another important aspect in fiscal policy.

Loans from the government, payment of interests and retirement of matured debts, all come under the purview of public debt management. Hence, fiscal policy is considered to be very crucial for the economy of India.

The role of fiscal policy varies as per the country's requirements. Developed countries make use of fiscal policy as an instrument to increase the level of employment and maintain stability in the economy. On the other hand, underdeveloped countries make use of fiscal policy to give a boost to economic growth.

As per **Buehler**, *"By fiscal policy is meant the use of public finance or expenditure, taxes, borrowing and financial administration to further our national economic objective."*

In the words of **Arthur Smithies**, *"Fiscal policy is a policy under which government uses its expenditure and revenue programmes to produce desirable effects and avoid undesirable effects on the national income, production and employment."*

Monetary policy

Monetary policy is referred to as the policy of Central Bank (RBI, in the context of India) of an economy in which the cost, availability and the usage of money are controlled and regulated by using monetary methods in order to achieve predetermined goals and objectives. It uses several tools to set the level of aggregate demand for goods and services or to assess the patterns and trends in the economic sectors.

The extent of economic activities and the supply and demand of flow of credit are influenced by the variations in the economy. These variations occur because of the amendments made in the monetary policy. Consecutively the monetary policy changes because of the varying availability and cost of credits. This change makes an impact on the asset pattern of commercial banks and financial institutions.

In the words of **Paul Einzig**, *"Monetary policy is the attitude of the political authority towards the monetary system of the community under its control."*

As per **Johnson**, *"Monetary policy is defined as policy employing central bank's control of the supply of money as an instrument for achieving the objectives of general economic policy."*

6.3.2.3 Legal environment

The legal environment in business is a code of conduct that defines the boundaries of business within a legal jurisdiction. The law has been meant to mean different things at different periods. Given below are some definitions**:**

Traditionalist approach: Legal traditionalists define law as a body of principles and rules that courts use during dispute resolution. As per them, no matter how much society changes its beliefs, the basic concepts of right and wrong will remain intact. □□

Environmental approach: Law is a tool used to control society. Thus, it must always demonstrate the moral constructs of the society through the execution of rules and regulations. This environmental approach is wider than the traditional viewpoint.

Social jurisprudence approach: Law is shaped by the society and its means of enforcement. It is a way to provide a systematic, predictable system of social order, change and legal reform.

Thus, the main objectives of the law are as follows: □□

- Maintain peace □□
- Deliver justice □□
- Provide equality and uniformity □□
- Protect individual rights □□
- Protect minorities against injustice □□
- Maintain social control □□
- Maintain law and order □□
- Resolve disputes □□

- Provide systematic
- Social change and legal reforms.

Acts influencing the Legal environment of business

The legal environment of business in India mainly comprises the legal policy, framework and laws in which businesses have to operate. These laws are enacted to protect the interests of both the producers and the customers.

- Indian Contract Act, 1872
- Sale of Goods Act, 1930
- Indian Partnership Act, 1932
- Companies Act, 2013
- Consumer Protection Act, 1986
- The Trade Marks Act, 1999
- The Patents Act, 1970
- The Information Technology Act, 2000
- The Indian Copyright Act, 1957

6.3.2.4 Socio-cultural environment

The socio-cultural environment includes social customs, values, codes of conduct, beliefs, traditions, etc. Every business is influenced by the socio-cultural environment; therefore, it is essential to examine the environment and make strategies accordingly. Education level of people, values and attitude, work ethics, family structure define social cultural environment. Social practice, beliefs and associated factors are helpful for promotion of the certain products, services or ideas; the success of marketing depends on a large extent, on the success in terms of changing social attitude or value systems.

Culture is a very crucial part of any business. There should be a proper understanding of the cultural dimensions for taking key business decisions. According to **E.B. Tylor**, *"Culture of civilisation is that complex whole which includes* *knowledge, belief, art, morals, law, customs and other capabilities and habits acquired by man as a member of society."*

Customs, traditions, values, beliefs, practices, behaviour, poverty, literacy, etc., that exist within a population comes under socio-cultural Environment. The social values and structure that society admires have a significant impact on the functioning of a business. For example, during Diwali, there is a huge demand for new clothes, sweets, fruits, flower, etc. Due to increase in literacy rate the consumers are becoming more conscious of the quality of the products. In addition, there has been a significant increase in consumerism. All these factors have led to tremendous increase in the demand for the different types of household goods. The consumption patterns, the dressing and living styles of people belonging to different social structures and culture vary significantly. This leads to generation of demands for different kinds of products.

The important socio-cultural factors that have a major impact on the operation of a business are as follows:

- **Culture:** According to the definition by House, Javidan et al., "culture is defined as shared motives values, beliefs, identities, and interpretations or meaning of significant events that result from common experiences of members of collectives and are transmitted across age generations." The culture that exists within a society or community has an overwhelming impact on any business. It has been an established fact that the culture drives people's behaviour, innovation and customer service.
- **Language:** Because of diversity, people in different state, countries use different languages to communicate. An organisation operating in different states or countries should have its business communication designed in a way that can be comprehended by the local audience. English is accepted as a universal business language.

- **Religion:** Religion even determines the way people think of work. As a result, religion influences enterprise and its operations. Many companies adapt their working processes according to a religion of a given state or countries in terms of the holidays, working hours, food habits, a way of dressing, etc.
- **Social systems:** The way individual interacts and socialises with other individuals in the society is called Social system. It includes family systems, marriage, caste system, etc. Social systems influence the consumption habit of people. For example, with an increasing number of families, the demand for fast foods and ready to cook foods has increased.
- **Level of education:** Education is about teaching, learning skills and knowledge. Education changes the lifestyle of people, their thoughts and the way of doing work. The level of education changes state-wise. However, in many countries, the level of education has a tendency to increase. The education level and level of literacy of population of a given country are indicators of the quality of their potential workforce.
- **Customer preferences:** With the spread of global communication and facilitated travel opportunities, certain social behaviours are getting similar globally. Today, people around the world watch the same movies, listen to the same music, play the same video games and use the same Internet websites. Apparently, the taste and habits of the population are becoming the same. This social trend is called global convergence.
- **Social institutions:** Social institutions such as family, economics, religion, education and state define the collective modes of behaviour. They prescribe a way of doing things. Secondary institutions are derived from primary institutions. The secondary institutions derived from family such as marriages, divorces, monogamy, polygamy, etc. The secondary institutions of education are school, college, university, etc. The secondary institutions of state are interest groups, party system, democracy, etc.

- **Population growth rate**: The increase in the number of individuals in a population. The rise in demand for food ultimately depletes natural resources needed by everyone for living.

6.3.2.5 Global environment

No matter wherever you are in the world, you are touched by globalisation. You may like it or hate it, but you cannot ignore it. Streets of New York or Old Delhi, you will find most of the people in denims. McDonald's is one of the most recognised brands in the world today, serving more than 119 countries. For the first time in the history of mankind, people-to-people exchange has spread to such a vast global level. On one end, they are working together in multinational corporations (MNCs) for shared goals, and on the other end, they are exchanging their culture and viewpoints on social media platforms.

There are myriad arguments for and against globalisation, but one thing is certain. Globalisation is here to stay because technologically, we've come too far and simply cannot remain isolated. Therefore, it is crucial that you understand the aspects and impacts of globalisation so that you can leverage it effectively for your business. This chapter describes the concept of globalisation and its impacts, modes of entries in the international market, types of international trade strategies, and the environment for foreign trade and investment. You will also learn about exchange rate movements and their impacts, globalisation trends and challenges, and balance of payment trends.

Globalisation and its impact on the Indian industry

Globalisation is defined as the rise in economic interdependencies on a global scale. It is an ongoing process that opens world markets and amalgamates societies and cultures. It dismantles the trade barriers between countries and increases the interchange of goods and services across nations. The main aspects of globalisation are:

- Alignment of local economies with global economies through free trade □□
- Foreign direct investment (FDI) flows □□
- Flow of capital □□
- Technological advancement □□
- Easier global communication □□
- Large-scale migration □□
- Sharing of cultural values □□
- Competitive advantage through easy access to low cost materials and labour
- Investment opportunities

Globalisation of the Indian economy started in 1991 after the Indian government took a series of economic reforms to resolve the severe balance of payment crisis. The Gulf War had just ended and India has to pay a massive import oil bill while the collections from exports were meagre. The total trade deficit was INR 17,369 crore. Making the crisis even more serious, India had made high-cost external commercial borrowings and non-resident deposits on which it was going to default. As a major policy change, the government of India initiated a new economic reform called Liberalisation, Privatisation, and Globalisation (LPG). The purpose of the LPG reform was to make the economy more efficient, fast growing, and globally competitive.

6.3.2.6 Technological Environment:

Technology is the most important factor which affects the business environment. Technology has changed the communication and system via internet and telecommunication. It has been changing the business trends and creating new business opportunities both in domestic and international market. Technological innovations help to adopt new ways of performing business tasks. E-Trading, e-retailing are a few emerging trends in today’s competitive business environment.

6.4 Emerging Sectors In Indian Economy

Emerging sector refers to an industry within an economy or a country that is in its initial stage of development, and is expected to grow rapidly in coming few years. The word sector may also be used for a group of industries. For example, economists generally divide all the industries in an economy in broad groups such agricultural, manufacturing and service sectors. So a sector of economy to qualify as emerging sector must satisfy two conditions. The first condition is that it is a sector which has established its presence but is not very big currently and the other condition is that it is currently growing fast and holds the promise to become an important sector of the economy in near future. Based on these two criterias the sectors, qualifying as emerging sector in Indian Economy today are Food Processing, Manufacturing Sector, Health Care, Organized Retailing, Education and Training, Tourism, Entertainment, Insurance, Knowledge Process Outsourcing etc. currently none of these sectors are very big, but they are growing very fastly and likely to become significantly bigger in near future. An industry qualifies as emerging sector, not only on the basis of its existing stage, but also on expectation of future growth.

- **Food processing**: The Indian food processing industry is a high priority sector and is poised for excellent growth in the coming years because it holds the vital link between agriculture and industry. India is the world's largest producer of food after China. With increasing impetus by the government on research, it is estimated that India's food production is likely to double in the next decade. This opens up huge opportunities in food processing areas like canning, packaging, frozen food and thermo processing. India is the world's largest producer of tea, sugarcane and milk. Processing industry is nascent stage but is growing rapidly. In India, the industry is largely dominated by ready to eat segment, which contributed nearly 90 percent of total sales of packaged foods in India.

Investment in the Indian food processing sector grew at 20 percent per annum in 5 years. The government is currently setting up 30 'Mega Food Parks' in 5 states which will exclusively cater to the food processing industry and also provides many sops and incentives. Despite being one of the largest producers of food, only 1.3 percent of food gets processed in India while nearly 80 percent is processed in developed world. Favourable factors like lower average age, higher levels of disposable income and increasing working couples have contributed to the success of this sector.

- **Information technology:** India is one of the leading exporters of IT services – driven mainly by the availability of a low-cost, English-speaking, qualified labour force. But huge gaps continue to exist on the supply side – the digital divide, for instance. While the urban population, with access to modern facilities, is increasingly getting used to computers, rural India is mostly starved of IT facilities. On the market side, India is facing competition from other countries such as China and may lose its current advantage if it does not move faster. Therefore, the challenge in IT will be to leverage India's strength of skilled, English-speaking manpower to remain a leader in the IT services arena.
- **Travel and Tourism** Currently, India has a very small share of the world tourism market. In 2000, India received a mere 2.6 million of the nearly 700 million international tourists. There are very good reasons why this number is so dismal. Current external sources of information do not portray a positive image of India. International tourists who visit India have a mixed experience. While most return satisfied with the variety of unique experiences India has to offer, safety, cleanliness, and quality of infrastructure still bother many. Therefore, returning visitors, by and large, describe their experience to others as "good, or even very good, BUT…". Quite clearly, attracting a larger number of international tourists and providing them with a high quality experience are the challenges for India.
- **Healthcare:** India's healthcare sector has been growing rapidly driven by a number of factors such as increasing the average life expectancy and average income level and rising awareness for health insurance. The Indian healthcare industry, which comprises hospitals, medicines, infrastructure, and medical devices, outsourcing telemedicine, health insurance and medical equipments is expected to reach US $100 billion by 2015 from the current US $65 billion, growing at around 20 percent year of year as per rating agency Fitch. Healthcare has become one of the

India's largest sectors both in terms of revenue and employment. Revenues from the healthcare sector account for 5.2 percent the GDP, making it the third largest growth segment in India. The sector's growth will be driven by the country's growing middle class, which can afford quality healthcare. Over 150 million Indians have annual incomes of more than US$ 1000, and many who work in the business services sector earns as much as US$ 20,000 a year. Today at least 50 million Indians can afford to buy Western medicines- a market only 20 percent smaller than that of UK. The growing purchasing power of Indian patients is revealed in the increase business of air ambulance services. Around 365 airlifting worth several millions of rupees happen in Delhi in a year on average.

- **Manufacturing sector:** The government has recently set up a National Manufacturing Competitiveness Council to examine the progressive reduction in taxes and tariffs, India emerging as a manufacturing hub manufacturing exports from India likely to grow to USD 450 billion in 2025 from USD 48 billion in 2003.
- **Food processing**: India is the world's largest producer of tea, sugarcane and milk processing industry is nascent but is growing rapidly FDI of 100% permitted except in special cases, capital goods can be imported freely. All profits from exports are free of corporate tax and minimum alternate tax.
- **The Indian telecom sector:** India is the fourth largest telecom market in Asia after China, Japan and South Korea. The Indian telecom network is the eighth largest in the world and the second largest among emerging economies. At current levels, telecom intensiveness of Indian economy measured as the ratio of telecom revenues to GDP is 2.1 percent as compared with over 2.8 percent in developed economies (CRISIL, www.ibef.com).Indian telecom sector has undergone a major process of transformation through significant policy reforms. The reforms began in 1980s with telecom equipment manufacturing being opened for private sector and were later followed by National Telecom Policy (NTP) in 1994 and NTP'1999. Historically, the telecom network in India was owned and managed by the Government considering it to be a natural monopoly and strategic service, best

under state's control. However, in 1990's, examples of telecom revolution in many other countries, which resulted in better quality of service and lower tariffs, led Indian policy makers to initiate a change process finally resulting in opening up of telecom services sector for the private sector.

- **Entertainment:** The last decade has seen the Indian entertainment industry grow exponentially. The key drivers for this have been technology and the government's recognition of the importance of the sector. The stage is now set for further evolution with a trend towards convergence, adding a new dimension to entertainment. The industry is expected to grow at a CAGR of 27 per cent. Revenues are projected to increase to US$ 10 billion in 2005 from 3 billion in 2002. India is one of the most media-exposed countries when compared to its Asian counterparts due to its size and consequently a large consumer base.
- **Retail:** Over the past few months, the retail sector has grabbed headlines with talks of 100% FDI in single brand retail, which is currently capped at 51%. While the outcome is still undecided, the opening up of India's retail will create a stronger, organised industry that will help in generating employment. Today, only a small part of retail in India is organised. Despite this, it is estimated that the sector in India is worth more than $400 billion, with domestic and international players planning to expand across the country. Industry leaders predict that the next phase of growth will emerge from rural markets. There are projections of the workforce doubling by 2025, from the current level in both organised and unorganised sector.

6.5 Check Your Progress

1. Which of the following is an important constituent of micro business environment?

A. Customers

B. Employees

C. Shareholders

D. All of these

2. Which micro business element provides raw materials for the process of production?

A. General public

B. Suppliers

C. Competitors

D. Marketing intermediaries

3. The business environment can be divided into:

A. National and local environment

B. Macro and micro environment

C. Financial and non-financial environment

D. Domestic and international environment

4. Macro business environment is beyond the control of a business. (**True/False**)

5. _________ policy implies the policy of the government regarding expenditure and tax.

A. Monetary

B. Fiscal

C. Industrial

D. All of these

6.6 Summary

- The business environment consists of a macro business environment and a micro business environment.
- Macro business environment is the general environment that affects the operations of all business entities in an economy. It cannot be controlled.
- Micro business environment is the immediate, specific environment in which an organisation operates. It can be controlled.
- Micro environment refers to the factors which directly influence the performance of the company.

- Components of micro business environment include customers, suppliers, competitors, marketing intermediaries, general public, employees and shareholders.
- The macro business environment consists of the political, economic, socio-cultural, technological, legal and natural environments.
- Business environment of an organisation is managed by environment scanning. It is the process of collecting and using information about occasions, patterns, trends and relationships within an organisation's micro and macro business environment.
- PESTLE analysis is used for macro environment scanning. It identifies the potential opportunities and threats arising from factors affecting the macro business environment.

6.7 Key Words

Gross Domestic Product: The value of all the goods and services produced in a country within a specific period of time.

Patent: A government authority/license bestowing a right/title for a specified period.

Statutory corporations: A corporation created by the state whose nature varies according to the jurisdiction.

Public sector: The part or sector of an economy that is controlled and regulated by the state.

Micro business environment: An environment comprised of various micro factors that affect business strategy, decision making and performance of an organisation.

6.8 Self Assessment Test

1. What is the macro business environment? Why is it important to a business?
2. What are the constituents of a macro business environment?
3. What factors impact the macro business environment? Illustrate with an example.
4. Why micro business environment is important for the business Organisation?

6.9 Answers To Check Your Progress

1. D
2. B
3. B
4. TRUE
5. B

6.10 Suggested/ Further Readings

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Privatization In India: Public Private Partnership

STRUCTURE

7.0 Learning Objectives

After going through this lesson, the learner should be able to:

- Know the meaning of public private partnership, and its models.
- Understand the objectives of public private partnership.
- Know the barriers, key issue and challenges for public private partnership.
- Understand the advantages and disadvantages of public private partnership.

7.1 Introduction

Public Private Partnership (PPP or 3P) have been highly controversial as funding tools, largely over concerns that public return on investment is lower than returns for the private fund provider. PPPs are closely related to concepts such as privatization and the contracting out of government services. The lack of a shared understanding of what a PPP is and the secrecy surrounding their financial details makes the process of evaluating whether PPPs have been successful complex. PPP advocates highlight the sharing of risk and the development of innovation, while critics decry their higher costs and issues of accountability. Evidence of PPP performance in terms of value for money and efficiency, for example, is mixed and often unavailable.

7.2 Public Private Partnership: Meaning

Public-private partnerships (PPPs) are a mechanism for government to procure and implement public infrastructure and/or services using the resources and expertise of the private sector. Where governments are facing ageing or lack of infrastructure and require more efficient services, a partnership with the private sector can help foster new solutions and bring finance. PPPs combine the skills and resources of both the public and private sectors through sharing of risks and responsibilities. This enables governments to benefit from the expertise of the private sector, and allows them to focus instead on policy, planning and regulation by delegating day-to-day operations. A public-private partnership (PPP) involves the private sector in aspects of the provision of infrastructure assets or of new or existing infrastructure services that have traditionally been provided by the government.

While there is no single definition of PPPs, PPP broadly refer to long-term, contractual partnerships between the public and private sector agencies, specifically targeted towards financing, designing, implementing, and operating infrastructure facilities and services that were traditionally provided by the public sector. These collaborative ventures are built around the expertise and capacity of the project partners and are based on a contractual agreement, which ensures appropriate and mutually agreed allocation of resources, risks and returns.

The Government of India defines a Public Private Partnership as: "Public Private Partnership (PPP) Project means a project based on a contract or concession agreement, between a Government or statutory entity on the one side and a private sector company on the other side, for delivering an infrastructure service on payment of user charges." In order to achieve a successful PPP, a careful analysis of the long-term development objectives and risk allocation is essential. The legal and institutional framework in the country also needs to support this new model of service delivery and provide effective governance and monitoring mechanisms for PPPs. A well-drafted PPP agreement for the project should clearly allocate risks and responsibilities. This definition provides the broad framework under which different kind of PPP models can be chosen from. A comprehensive listing of various models is discussed in this report.

7.3 Public Private Partnership Models

The range of options for public-private partnerships has expanded enormously over the past 30 years. Agreements between public and private entities take many shapes and sizes for both new and existing services. At one end of the spectrum is a management or service contract, where a private company is paid a fee for a service. At the other end PPP is full privatization or divestiture (outright sale), where a government sells assets to a private company. Outsourcing has become another popular option; here a private company might handle an aspect of service, such as billing, metering, transport, or even cleaning. Hybrid models of public-private partnership have seen explosive growth in recent years, especially with the development of a more diversified pool of emerging market investors and operators with local expertise. These models often rely on simpler contractual arrangements and blend public and private money to diversify risks.

A large variety of PPP formats have been documented as:

Design Build (DB): Under this model, the government contracts with a private partner to design and build a facility in accordance with the requirements set by the government. After completing the facility, the government assumes responsibility for operating and maintaining the facility. This method of procurement is also referred to as Build-Transfer (BT).

Design Build Maintain (DBM): This model is similar to Design-Build except that the private sector also maintains the facility. The public sector retains responsibility for operations.

Design Build Operate (DBO): Under this model, the private sector designs and builds a facility. Once the facility is completed, the title for the new facility is transferred to the public sector, while the private sector operates the facility for a specified period. This procurement model is also referred to as Build-Transfer-Operate (BTO).

Design Build Operate Maintain (DBOM): This model combines the responsibilities of design-build procurements with the operations and maintenance of a facility for a specified period by a private sector partner. At the end of that period, the operation of the facility is transferred back to the public sector. This method of procurement is also referred to as Build Operate-Transfer (BOT).

Build Own Operate Transfer (BOOT): The government grants a franchise to a private partner to finance, design, build and operate a facility for a specific period of time. Ownership of the facility is transferred back to the public sector at the end of that period.

Build Own Operate (BOO): The government grants the right to finance, design, build, operate and maintain a project to a private entity, which retains ownership of the project. The private entity is not required to transfer the facility back to the government.

Design-Build-Finance-Operate/Maintain (DBFO, DBFM or DBFO/M): Under this model, the private sector designs, builds, finances, operates and/or maintains a new facility under a long-term lease. At the end of the lease term, the facility is transferred to the public sector. In some countries, DBFO/M covers both BOO and BOOT. PPPs can also be used for existing services and facilities in addition to new ones. Some of these models are described below.

- **Service contract:** The government contracts with a private entity to provide services the government previously performed.

- **Management contract:** A management contract differs from a service contract in that the private entity is responsible for all aspects of operations and maintenance of the facility under contract.

- **Lease:** The government grants a private entity a leasehold interest in an asset. The private partner operates and maintains the asset in accordance with the terms of the lease.

- **Concession:** The government grants a private entity exclusive right to provide operate and maintain an asset over a long period of time in accordance with performance requirements set forth by the government. The public sector retains ownership of the original asset, while the private operator retains ownership over any improvements made during the concession period.

- **Divesture:** The government transfers an asset, either in part or in full, to the private sector. Generally the government will include certain conditions with the sale of the asset to ensure that improvements are made and citizens continue to be served.

7.4 Types Of PPP Arrangement

Among different possible classifications, PPPs can be categorized into two types: a PPP of a purely contractual nature and a PPP of an institutional nature. This categorization is adopted by the European Union and by many other countries. In a PPP of a purely contractual nature, the partnership between the public and the private sector is based solely on contractual links, whereas in a PPP of an institutional nature there is cooperation between the public and the private sectors within a distinct entity. Both arrangements involve delegated management of the traditional public sector activities to the private sector. In the first type of PPP, the rights and obligations are regulated by an administrative contract or series of contracts. In the second, these are guaranteed by the company's statutes and by the shareholder agreement between public and private parties. There is contractual regulation in both situations.

Contractual PPPs*:* In the scope of purely contractual PPP, there are different kinds of arrangements that depend on the characteristics of the contractual relationship and delegation of tasks to the private partner. Some of the best known models are in the development of urban infrastructure facilities: the associated provision of services corresponds to the "concession model". In this situation there is a direct link between the private partner and the final user: the private partner provides a service to the public "in place of", though under the control of, a public authority. The private party assumes all the responsibility relative to the construction, operation and maintenance of the infrastructure assets, charging users for the service. Usually the concession model is associated with long contractual periods, matching the long asset life of infrastructure.

An important variant of the contractual PPP relates to infrastructure systems where it becomes necessary to transfer funds from the government or other external entities (e.g. donors) to assure their economic-financial balance. This model, known as PFI (private finance initiative), was initially aimed at sectors such as health (hospitals) or education (schools) where there was a periodical payment (monthly or annual) to the private partner for making that infrastructure available. This model has been extended to many other sectors (e.g. in transportation, shadow tolls) and can perform a valuable role both in developing countries where cost recovery through users is socially complicated and in segments of the urban infrastructure systems production process (e.g. water or wastewater treatment plants). A plethora of different kinds of contractual PPPs and new variations emerge continuously as each PPP contract responds to very precise needs. Some of the most frequent labels are BOT (build, operate and transfer); that is, the private partner builds and operates the infrastructure, transferring it for the public partner at the end of the contract. BOOT (build, own, operate, and transfer) is the organizational form when infrastructure ownership is also private during the contract term; DBOT or DBOOT would be the acronyms if arrangements further include the responsibility for the design of the infrastructure project as well. The concession model is also, sometimes, separated into public works and public service concessions, depending on the business (contract) value of the infrastructure or service provision, respectively. In fact, many concessions are of mixed type: there is a balance between both activities.

Leasing/afterimages: A variation of the PPP concession model is afterimage (or leasing) contracts. This model is analogous to the concession model, except for investment in and financing of the infrastructure assets, which are under the responsibility of the public and not the private partner. This form of contractual PPP can be appropriate in situations where assets have already been building and it is not necessary to make investments in infrastructure or where the risk premium of transferring this responsibility to the private partner is very high. The commercial risk continues, a priori, to be allocated to the private party and the contract length is often shorter than in the case of a concession (in general between 10 and 18 years).

Delegated management contracts: Another format of contractual PPP is delegated management contracts, which are at the boundary of PPPs depending on the risk transferred in each situation. They encompass relatively short periods (3 to 8 years); the payment of the private partner is done by the public partner (rather than involving revenue collection directly from the end consumer), often according to the service delivered (e.g., drinking water treatment plant operation is paid based on the quantity of drinking water treated). This arrangement is basically service provision through outsourcing; although some of the PPP principles apply to this case (e.g. output orientation), it is not a “true partnership”. Delegated management contracts are often used in preparation for more fully involved PPP contracts, e.g. long-term concession contracts, or even divestitures.

Institutionalized PPPs: Institutionalized PPPs (mixed companies) imply the establishment of an entity held jointly by the public partner and the private partner. The joint entity thus has the responsibility of ensuring the delivery of a work or service for the benefit of the public. The establishment of an institutionalized PPP can be done either through an entity where public and private sectors jointly participate or through private sector buying and owning shares in an existing public company. Usually the public partner controls the company either as shareholder or through special rights it may hold and the private partner operates the service. This kind of cooperation between public and private partners can be very positive since the public partner keeps control over the infrastructure service, it may allow for service adjustment over time according to changing needs, conflicts are resolved internally and the public partner acquires know-how from the joint work with the private party.

Notwithstanding the existence of a sector regulator, what regulate the PPP are the company statutes and the shareholder agreement. The statutes of the company establish common rules for the organization, governance and operation of the company. The shareholder agreement regulates relationships between partners (public and private). This last document is central to the performance of the entity. It establishes the minimum financial participation required by the private partner, risk sharing arrangement, the procedures to be used in a deadlock situation, and the possibility of a call-option by the public entity, placing pressure on partners to perform well during the PPP contract period. In the same way there are several advantages in the fact that the public partner can have a more active and participating role in this PPP model, being able to limit conflicts and better solve difficulties, the institution is susceptible to “capture”. Due to close contact or identification with partner concerns, those representing the public might become excessively attached to the objectives of the private partner, thus harming the public interest.

7.5 Objectives Of Public Private Partnership

While many governments have reformed their utilities without private participation, some seek finance and expertise from private companies to ease fiscal constraints and increase efficiency. By engaging the private sector and giving it defined responsibilities; governments can broaden their options for delivering better services. PPP’s can emerge as a win-win for the public as well as the private sector and most importantly, the citizen. PPP’s seek to address limitations of both the sectors and the main reasons for PPP projects’ increased importance are:

- **Limited resources and finances:** Limitations of government resources and limited capacity to meet the infrastructure gap.
- **Need for different institutional mechanisms:** This includes incorporating the spirit of private efficiency into providing services for the public.
- **Equitable risk allocation and mitigation:** Shared risk allocation is a principal feature of a PPP project. PPP projects allow sharing of different kinds of risks between the private and public sector.
- **Complementary roles and drivers:** Putting it somewhat simplistically, the public sector is predominantly driven by the ‘public good’, the private sector by ‘profit’. PPP

projects allow both the sectors to cooperate and make these seemingly contradictory goals work together. As an example, land acquisition and environmental clearances are best obtained by governments, and the private sector can deliver much faster, if such clearances are handled by the government.

According to Asian Development Bank, the three main needs that motivate governments to enter into PPP's for infrastructure are:

1. To attract private capital investment (often to either supplement public resources or release them for other public needs);

2. To increase efficiency and use available resources more effectively; and

3. To reform sectors through a reallocation of roles, incentives, and accountability.

7.6 Key Issues And Challenges For PPP In India

There are many challenges for implementation of public-private partnership projects:

- **Commercial viability** - Projects as water supply and sanitation projects are yet to demonstrate their commercial viability to the public.

- **Contractual and capacities imbalance -** Insufficient experience of the partners, particularly of the public sector while contracting such projects, where we can notice an informational asymmetry operating in favor of private companies, which naturally use their endeavor and potential to negotiate better conditions for themselves.

- **Hidden debt -** From the macro-economic point of view, we can see a substantial disadvantage in the fact that as a consequence of the long-term character of PPP projects, the mandatory expenses grow and the hidden debt arises, and this debt will exist for a lot of years, and thus it can affect negatively the fighting power of the future governments and burden significantly the future generations.

- **Long gestation period -** Generally the preparation of individual PPP Projects may take up to 2- 3 years (depending on project size and complexity). This long gestation period along with its attendant uncertainties are a big dampener for private sector enthusiasm.

• **Breaking of partnerships -** Considerably negative financial impacts in the case the partnership has to be repudiated.

• **Transfer of risk -** From the private sector to the public sector possible a new set of risks, e.g. possible risk of bankruptcy of the private player.

• **Focus on economic benefits -** PPP Projects tend to focus on the economic aspects of the project, sometimes to the detriment of social and environmental aspects.

7.7 Barriers To Public Private Partnership (PPP)

Mr. P. Chidambaram (Finance Minister in 2006), in a major PPP Conference listed four major weaknesses in PPP development in India as:

- **Weakness in enabling policy and regulatory framework:** Substantial work need to be done in making sector policies and regulations PPP friendly. A large number of these projects are in the States and without the active participation of the States it would not be possible to achieve satisfactory results.
- **Lack of long term instruments:** The market presently does not have adequate instruments and capacity to meet the long-term equity and debt financing needed by infrastructure projects.
- **Lack of bankable projects:** Finding credible and viably structured projects continues to be a challenge. There is a lack of shelf of credible, bankable infrastructure projects, which could be offered for financing to the private sector. Some initiatives have been taken both at the central as well as the states' level to develop PPP projects these tend to be isolated cases and have demonstrated a marked lack of consistency.
- **Limited capacity to manage PPP in public sector:** There is also lack of capacity in public institutions and officials to manage the PPP process. Since these projects involve long term contracts covering the life cycle of the infrastructure asset being created, it is necessary to manage this process to maximize returns to all the stakeholders.
- In addition to these, the other obstacles include:

- **Lack of political will:** PPP contracts are often seen as government 'selling its jewels'. This myth is perpetuated partly by the political parties for maintaining vested interests, and partly by inefficient or corrupt bureaucracy which is sometimes reluctant to part away with operational control. Paradoxically the honest bureaucrat finds that 'selling' the PPP concept is more hard work than the actual implementation and also makes him / her vulnerable to charges of corruption and nepotism.
- **Varied institutional framework:** Every state has varied institutional framework especially the regulatory framework developed by different states. States like Andhra Pradesh, Gujarat, and Punjab have legislation which clearly defines what infrastructure is and how these infrastructure projects are going to be executed by the private sector. Other states have differing administrative (instead of legislative) frameworks in place for decision-making. These divergent institutional frameworks, prevents fast tracking of projects since major clearances are still required from GOI who have to deal with this multiplicity.
- **Non standardization of procurement procedures:** Prequalification, bidding, and procurement procedures are not standardized across States, sometimes not even across Ministries. This again slows down the clearances and approval procedures.
- **Need for balancing transparency with expediency:** Demand for ensuring transparent relationships and transactions, whether while selecting a partner, or defining the terms and conditions, competences and responsibilities or while concluding contracts itself makes the PPP contracts' conclusion a very arduous and time consuming process. While RTI is an excellent means to ensure transparency, its misuse in some cases and the perceived threat of persecution, also delays PPP project design and implementation.
- **Absence of rigorous project development**: A key impediment to successful commercialization of projects in India has been the absence of rigorous project development. Many of the projects bid out by the government have been ill defined, inadequately structured, and unsuitable for PPP.
- **Public sector capacity to successfully execute PPPs**: Perhaps the single biggest reason for delays and sub optimal framing of PPP projects has been the public sector's limited skills set and experience in drafting balanced PPP contracts and concession agreements.

- **Risk and return concerns**: Need to address the Risk and Return Concerns of Foreign Investors. Financing terms generally mean that PPP's are more exposed to interest rate volatility— this causes concern in a period of rising rates and reduced liquidity.
- **Decentralization and devolution**: Water Supply and Sanitation (WSS) is a state/municipal subject in India, whereby the Constitution mandates that the responsibility of providing WSS services should vest with the respective city Government. However, given the traditional division of roles and responsibilities, and budget flow mechanisms, this responsibility has not been fully transferred to local bodies in many states. This results in a multi-layered political structure being involved in decision-making in the sector. This is further complicated by political economy issues in the designing of PPP projects in the WSS sector.

7.8 Advantages and Disadvantages Of Public-Private Partnerships

Partnerships between private companies and government provide advantages to both parties. Private-sector technology and innovation, for example, can help to provide better public services through improved operational efficiency. The public sector, for its part, provides incentives for the private sector to deliver projects on time and within budget. In addition, creating economic diversification makes the country more competitive in facilitating its infrastructure base and boosting associated construction, equipment, support services, and other businesses.

There are downsides too. Physical infrastructure, such as roads or railways, involves construction risks. If the product is not delivered on time, exceeds cost estimates, or has technical defects, the private partner typically bears the burden. In addition, the private partner faces availability risk if it cannot provide the service promised. A company may not meet safety or other relevant quality standards, for example, when running a prison, hospital, or school. Demand risk occurs when there are fewer users than expected for the service or infrastructure, such as toll roads, bridges, or tunnels. If the public partner agreed to pay a minimum fee no matter the demand, that partner bears the risk.

7.9 Public-Private Partnership: Examples

Public-private partnerships are typically found in transport infrastructure such as highways, airports, railroads, bridges, and tunnels. Examples of municipal and environmental infrastructure include water and wastewater facilities. Public service accommodations include school buildings, prisons, student dormitories, and entertainment or sports facilities.

7.10 Check Your Progress

Multiple Choice Questions:

1. The main characteristic of PPP is

A. long term (sometimes up to 30 years) service provisions

B. The transfer of risks to the private sector

C. different forms of long-term contracts drawn up between legal entities and public authorities.

D. All of the above

2. What is the ingredient common to all types of PPP

A. The public sector transfers the overall responsibility to provide the public service

B. value for money will be the basic criterion for the public sector

C. No balanced sharing of the risks and gains between the public sector and private

D. none of the above

3. The National highway projects contracted out by NHAI under PPP is an example of

A. LOT

B. BOOT

C. BOT

D. DBFO

4. The common characteristic of Institutional PPPs and contractual PPPs is

A. The operation of a facility is contracted out to another private party

B. The users pay for the facility availed and such charges accrue to the private sector partner

C. The public sector usually designs, constructs and operate PPP

D. None of the above

5. What distinguishes each type of PPP model from one another is

A. The degree of risk and responsibility borne by the private sector partner

B. The degree of risk and responsibility borne by the public sector

C. The private sector partner will bring in most of the investment requirements

D. None of the above

6. The main difference between PPP and privatization is

A. There is no permanent transfer of ownership of assets to private partner

B. The responsibility and accountability to deliver the goods and services remains with the state/public sector

C. Besides the transfer of ownership to the private sector, the accountability is also shifted to the purchaser

D. None of the above

7. Find out the incorrect statement

A. The private sector partner should equally gain from the innovation brought about by it

B. The private entrepreneurs come into the PPP arrangements primarily with profit motive

C. PPP projects are aimed to provide 'improved' public services by transferring the risks to the private sector

D. None of the above

7.11 Summary

Public-private partnership (PPP), partnership between an agency of the government and the private sector in the delivery of goods or services to the public. Areas of public policy in which public-private partnerships (PPPs) have been implemented include a wide range of social services, public transportation, and environmental and waste-disposal services. Although PPPs are an ancient phenomenon but were not studied seriously by scholars until the late 1980s, when they began to be adopted in public administration and management in both developed and developing countries. PPPs have been a topic of political controversy and scholarly debate, especially regarding the advantages and disadvantages of PPPs in comparison with traditional government-run services and the nature of the partnerships they bring about.

In its most basic sense, a partnership is any business or institutional association within which joint activity takes place. A PPP exists from the moment one or more public organizations agree to act in concert with one or more private organizations. PPPs embrace public-sector partnerships with both businesses and organizations in civil society, including community organizations, voluntary organizations, and nongovernmental organizations (NGOs). PPPs have been widely adopted. Indeed, in many developed countries (e.g., the United States, the United Kingdom, France, Italy, and the Netherlands), their use has been mandated through legislation. In France, for example, the PPP concept is of quite long standing, and, since the 1980s, PPPs have been implemented in almost all areas of public policy.

7.12 Key Words

Public Private Partnership (PPP, 3P): Public-private partnerships (PPPs) are a mechanism for government to procure and implement public infrastructure and/or services using the resources and expertise of the private sector.

DBO: Design Build Operate

BOOT: Build Own Operate Transfer

BOO: Build Own Operate

DBOM: Design Build Operate Maintain

7.13 Self-Assessment Test

Q.1 Explain about public private partnership and different models of public private partnership.

Q.2 Write the advantages and disadvantages of public private partnership.

Q.3 Explain about main barriers and key issues for PPP in India.

7.14 Answer To Check Your Progress:

1. (D), 2. (B), 3. (C), 4. (B), 5. (A), 6. (B), 7. (C)

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Course: Business Environment	
Course Code: **MBA 105**	Author: **Dr. Rajiv Kumar**
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Challenges And Opportunities In Rural Sectors

STRUCTURE

8.0 Learning Objectives

8.1 Introduction And Definition Of Rural Markets

8.2 SWOT Analysis Of Rural Markets

8.3 Initiatives That Can Be Taken By Corporate Bodies To Tap The Rural Market

8.4 Marketing Challenges In Rural India

8.5 Marketing Opportunity In Rural Sector In India

8.6 Reasons For Corporate Interest In Rural Markets

8.7 Recent Developments In Rural Areas

8.8 Government Initiatives To Improve Infrastructure In Rural Areas

8.9 Rural Segment Quickly Catching Up

8.10 Future Road Map Of Rural Sector

8.11 Check Your Progress

8.12 Summary

8.13 Keywords

8.14 Self Assessment Test

8.15 Answers To Check Your Progress

8.16 Suggested/Further readings

8.0 LEARNING OBJECTIVES

After going through this lesson, the learners should be able to:

- Understand the growing interest and enthusiasm of business towards rural markets
- To understand the problems of rural sector in India.
- To examine the opportunities in rural market.
- To assess the role of govt. in the rural economy.
- To analyse the market from urban to rural, rural to urban and within the rural market.

8.1 INTRODUCTION AND DEFINITION OF RURAL MARKETS

Opportunities in the rural market are examined in the light of intense and growing competition in urban markets. The market opportunities are clearly perceived through a comparison of consumption patterns for durables as well as non-durables between the rural and urban markets. Identifying opportunities and clarity in decision-making requires an unambiguous definition of rural marketing. Marketing challenges in rural areas are also discussed. Recent developments and government initiatives taken to improve infrastructure in rural areas are discussed in this chapter.

India's vast rural market offers a huge potential for a marketer facing stiff competition in the urban markets. The rural market environment is very different from the familiar surroundings of the urban market. Rural consumers have customs and behaviour that the marketer may find difficult to contend with. According to the national commission on agricultural: 'Rural marketing is a process which starts with a decision to produce a saleable farm commodity and it involves all the aspects of the market structure or system, both functional and institutional, based on technical and economic consideration which includes pre & post-harvest operations, assembling, grading, storage, transportation and distribution. FMCG sector identified "Rural" as place with a population less than or equal to 20,000 peoples.

FMCG refers to consumer non-durable goods required for daily or frequent use and move fast at the sales counter. Normally consumer devotes less time and efforts in buying these goods. FMCG are relatively high volume and low value products. The FMCG sector consists mainly of sub segment viz., personal care, oral care and households products. Rural marketing signifies those business activities that bring in the drift of goods from urban sectors to the rural regions of the country as well as the marketing of non-agriculture merchandises from rural to urban areas. The important characteristics of rural market are as follows: The rural market has been experiencing a considerable change over the last few decades. This is the result of generation of new employment opportunities and new source of income made accessible through various rural development programmes. The rural markets are by and large less discovered, less exploited and largely agriculture oriented.

The rural markets are characterised by small purchasing power and low per capita income clubbed with high sense of savings, low literacy rate resulting in low standard of living. In addition to this, the traditions, religious pressure and cultural values are the hindering factors for an upwards social mobility. Apart from this, the distribution of income varies considerably due to the variation in the landholding pattern. Thus rural population presents a highly heterogeneous market. The purchasing powers of the people in the rural areas mainly depend upon marketable agricultural surplus and rural-urban trade. Increase in marketable surplus of food grains leads to the consumption of manufactured consumer goods. To a larger extent Indian agriculture depend on rainfall and therefore, rainfall indirectly influences the rural demand for consumer goods.

8.2 SWOT ANALYSIS OF RURAL MARKETS

Internal Factors	**Strength**	**Weakness**
	1. Large Indian population 2. Good government support	1.Lack of good Infrastructure 2. Lack of physical

	3. Availability of Products, Raw Material 4. Working labour in abundance	distribution network 3. Low consumption level 4.Less Research and Development
External Factors	**Opportunities**	**Strategies**
	1. Growing Income Levels of Rural Consumers 2.Growing Literacy Levels **3**. Growing quality Consciousness Strategies **4**.Changing Socio Economic Scenario.	1. Customization of Products according to rural consumer demographics. **2**. Strengthening of supply chain system with government support and infrastructure. **3**. Launching of Branded Products in rural markets due to increasing literacy rate and brand awareness.
	Threats	**Strategies**
	1. Increasing Grey Market **2**. Growing Competition **3**. Less Knowledge levels on Product Identification	**1**. Educate rural consumers on Product quality and usage **2**.Implementation and Amendment of laws /rules/regulations to control the Grey Market **3**.Product Awareness using rural media

8.3 INITIATIVES THAT CAN BE TAKEN BY CORPORATE BODIES TO TAP THE RURAL MARKET

1. A marketing strategy which is massively unexploited by most of the companies is employing the villagers themselves to market the products. HUL has been the pioneer in this form of marketing. HUL has initiated the Shakti campaign where women in villages are employed to form a delivery network of HUL products in the rural areas. Employing local people for marketing particularly in areas where it is challenging to commute was an innovative way to increase accessibility and marketing of the Bottom of the Pyramid (BOP) products.

2. Electricity Can Be Replaced By Solar Energy: Though electricity is one of the major hindrances in rural areas the problem can be overcome by extensive use of solar energy.

3. For progressing product strategies, the marketers should think in terms of low unit price and low volume packing's which convey a perception of sturdiness and utility in the minds of rural consumers. Whenever necessary, redesigning of the product can also be thought of depending on the customs, traditions, proscriptions and habits, of rural customers.

4. Pricing strategies are closely associated to the product strategies. The product packaging and presentation also offer scope for keeping the price low to suit the rural purchasing power.

5. The marketers aim to reduce the value of the product to a reasonable level, so that a bigger segment of the population can purchase it, thus intensifying the market.

6. For construction of distribution strategies in rural areas, it is necessary to keep in mind; the physiognomies of the product, consumable and non-consumable, and life cycle and other factors relating to distribution.

7. The marketers may distribute the products through Co-operatives societies and by utilising the services of Public Distribution System, developing of multi-purpose distribution centres by Petroleum /Oil companies, distribution up to the feeder markets/mandi towns, haats/melas, and agriculture input dealers.

8. The promotional measure or strategies picked should be cost effective, while consumable products may warrant the usage of mass media since the target consumers are substantial, durable products will require personal selling efforts because of smaller size of target.

8.4 MARKETING CHALLENGES IN RURAL INDIA

1. **Deprived people and deprived markets:** The number of people below the poverty line has not decreased in any appreciable manner. Thus, poor people and consequently underdeveloped markets characterize rural markets. A vast majority of rural people is tradition bound, and they also face problems such as inconsistent electrical power, scarce infrastructure and unreliable telephone system, and politico-business associations that hinder development efforts.
2. **Lack of communication facilities:** Even today, most villages in the country are inaccessible during the monsoons. A large number of villages in the country have no access to telephones. Other communication infrastructure is also highly underdeveloped.
3. **Transport:** Many rural areas are not connected by rail transport. Many roads have been poorly surfaced and got severely damaged during monsoons. The use of bullock carts is inevitable even today. Camel carts are used in Rajasthan and Gujarat in both rural and urban sectors.
4. **Many languages and dialects:** The languages and dialects vary from state to state, region to region and probably from district to district. Since messages have to be delivered in the local language, it is difficult for the marketers to design promotional strategies for each of these areas. Facilities such as phone, telegram and fax are less developed in villages adding to the communication problems faced by the marketers.
5. **Low per capita Income:** The per capita income of rural people is low as compared to the urban people. Moreover, demand in rural markets depends on the agricultural situation, which in turn depends on the monsoons. Therefore, the demand is not stable or regular. Hence, the per-capita income is low in villages compared with urban areas.
6. **Prevalence of spurious brands and seasonal demand:** For any branded product, there are a multitude of local variants, which are cheaper and hence more desirable. Also, due to illiteracy, the consumer can hardly make out a spurious

brand from an original one. Rural consumers are cautious in buying and their decisions are slow, they generally give a product a trial and only after complete satisfaction they buy it again.

7. **Warehousing problem:** Warehousing facilities in the form of godowns are not available in rural India. The available godowns are not properly maintained to keep goods in proper conditions. This is a major problem because of which the warehousing cost increases in rural India.

8. **Problems in sales force management:** Sales force is generally reluctant to work in rural areas. The languages and dialects vary from state to state, region to region, and probably from district to district. Since messages have to be delivered in the local language, it is difficult for sales force to communicate with the rural consumers. Sales force finds it difficult to adjust to the rural environment and inadequate facilities available in rural areas.

9. **Distribution problem:** Effective distribution requires village-level shopkeeper, taluka-level wholesaler/dealer, district-level stockist/distributor, and company-owned depot at state level. These many tiers increase the cost of distribution. Rural markets typically signify complex logistical challenges that directly translate into high distribution costs. Bad roads, inadequate warehousing and lack of good distributors pose as major problems to the marketers.

8.5 MARKETING OPPORTUNITY IN RURAL SECTOR IN INDIA

1. **IT penetration in Rural India:** Today's rural children and youth will grow up in an environment where they have information access" to education opportunities, job opportunities, government schemes, and worldwide news and mandi prices. Rural areas offer a great potential for growth in internet usage with the number of claimed internet users.

2. **Reduction of risk during recession**: It has been observed that companies which cater both urban and rural markets tackle the recession in the better way. The demands for goods in the urban market often follow a cyclic whereas in the rural

market it is steady. So companies can safeguard themselves from the harmful effects of recession after entering in the rural market**.**

3. **Increase population and hence increase in demand**: The rural market in India is vast and scattered and offers a plethora of opportunities in comparison to the urban sector. It covers the maximum population and regions and thereby, the maximum number of consumers.

4. **Increase in literacy rate:** Literacy rate is increasing in rural areas. According to census 2011, there are more graduates in rural than in urban India. This brings social and cultural changes in buying behaviour of the rural customers and more aware about national and international brand. Due to increase in literacy rate they get jobs in nearby towns. They earn urban salaries but continue to live in self owned homes in the villages, they have high purchasing power and prefer to buy branded product.

5. **Increasing in disposable income and purchasing power:** Projects from private companies and the rural employment initiatives by the Government like MNREGA (Mahatma Gandhi National Rural Employment Guarantee Act) schemes have given the rural population an opportunity to meet their daily needs. Government decided to expand the agriculture loan at lower rate of interest and distribute million of Kisan Credit Cards, has given a boost to the income level to the rural sector.

8.6 REASONS FOR CORPORATE INTEREST IN RURAL MARKETS

1. **Untapped potential:** Rural markets offer a great potential for marketing branded goods and services because of the large number of consumers. That reflects the larger volume sales of certain products in rural areas as compared to sales of the same products in urban areas. The penetration levels for many products are low in rural areas.

2. **Market size, penetration and potential:** India's per capita GDP in rural regions has grown at a Compound Annual Growth Rate (CAGR) of 6.2 per cent since 2000. The Fast Moving Consumer Goods (FMCG) sector in rural and semi-urban

India has crossed US$ 20 billion mark in 2018 and expected to reach US$ 100 billion by 2025.

3. Unmet needs/low penetration: Increase in the consumption of various types of products in rural markets creates opportunities for marketers. Moreover, products that were considered suitable only for urban markets are now in demand in rural markets as well.

4. Current consumption a pointer to potential: The purchase and use of certain durables and non-durables by consumers in rural areas is more than that by consumers in urban areas. Some of these items are sewing machine, cassette recorder, radio/transistor, bicycle, wristwatch, table fan, black-and-white television and pressure cooker etc.

5. Increasing income and purchasing power: The agriculture development programmes of the government have helped to increase income in the agriculture sector. This, in turn, has created greater purchasing power in rural markets. Studies by NCAER provide evidence of the increased income of rural households. Households in the lower income group have become less while there is a strong growth in the number of upper middle and higher income households.

6. Accessibility of markets: The attraction of a market depends not only on its potential but also on its accessibility. A market that cannot be exploited is a case of 'sour grapes'. The development of infrastructure facilities and marketing institutions has increased the accessibility of these markets.

7. Competition in urban markets: Intensified competition in urban markets increases costs and reduces market share. Rural markets are, therefore, increasingly attractive in relation to urban markets. The automobile market brings this out clearly. Motorcycles, certain models of scooters and vans find ready acceptance in rural markets as compared to urban markets, where there is a proliferation of brands.

8. Consumer behaviour changes: Increased literacy and greater awareness in rural markets create new demands and discriminating buyers. This is observed more in the younger generation. In villages today, this segment of buyers consumes a large variety of products, both durable and non-durable. There is a visible increase in the consumption and use of a variety of products. The younger generation appears to seek variety and is more discriminating.

8.7 RECENT DEVELOPMENTS IN RURAL AREAS

Following are some of the major investments and developments in the Indian rural sector.

- India's unemployment rate has declined to 4.8 per cent in February 2017 compared to 8.5 per cent in August 2016, as a result of the Government's increased focus towards rural jobs and the Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA) scheme.
- The Ministry of Rural Development is expecting to achieve its annual targeted length of 48,812 kilometers of rural roads by March 31, 2017 under the Pradhan Mantri Gram Sadak Yojana (PMGSY), which has reached a completion stage of 67.53 per cent (32,963 kms) as on January 27, 2017.
- The National Bank for Agriculture and Rural Development (NABARD) plans to provide around 200,000 point-of-sale (PoS) machines in 100,000 villages and distribute RuPay cards to over 34 million farmers across India, to enable farmers to undertake cashless transactions.
- Magma Fincorp, a Kolkata-based non-banking finance company (NBFC) plans to expand its operations in South India, with specific focus on rural and semi-urban markets to help the company grow rapidly.
- Bharti Airtel is applying for a payments bank licence and has involved Kotak Mahindra Bank as a potential investor in the venture, in a bid to tap significant revenue opportunities from the Reserve Bank of India's financial inclusion initiative. Payments banks are meant to fan out into the rural, remote areas of the country, offering limited but critical services such as

money transfers, loans and deposit collection. While banks have the knowhow, telecom companies have the network, making it an ideal match.

8.8 GOVERNMENT INITIATIVES TO IMPROVE INFRASTRUCTURE IN RURAL AREAS

The Government of India has planned various initiatives to provide and improve the infrastructure in rural areas which can have a multiplier effect in increasing movements of goods, services and thereby improve earnings potential of rural areas subsequently improving consumption.

- The Government of India has approved the proposal to construct 10 million houses for the rural population, which will require an investment outlay of Rs 81,975 crore (US$ 12.7 billion) for the period from 2016-17 to 2018-19.
- The Government of India aims to provide tap water regularly to every household by 2030 in line with United Nations Sustainable Development Goals, requiring a funding of Rs 23,000 crore (US$ 3.57 billion) each year until the target is met.
- The Government has introduced various reforms in the Union Budget 2017-18 to uplift the rural markets. Some of the key highlights of the Budget are:
    - Rs 187,223 crore (US$ 28.08 billion) has been allocated towards rural, agriculture and allied sectors.
    - The Allocation for Pradhan Mantri Aawas Yojana-Gramin has been increased from Rs 15,000 crore (US$ 2.25 billion) to Rs 23,000 crore (US$ 3.45 billion) in the year 2017-18 with a target to complete 10 million houses for the houseless by the year 2019.
    - The pace of roads construction under Pradhan Mantri Gram Sadak Yojana (PMGSY) has been accelerated to 133 kms per day as against an average of 73 kms per day during the years 2011-14.

- The allocation to the Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA) has been Rs 48,000 crore (US$ 7.2 billion) in the year 2017-18, which is the highest ever allocated amount.
- The Government of India is looking to install Wi-Fi hotspots at more than 1,000 gram panchayats across India, under its ambitious project called Digital Village, in order to provide internet connectivity for mass use, as well as to enable delivery of services like health and education in far-flung areas.
- In the Union Budget 2017-18, the Government of India mentioned that it is on course to achieve 100 per cent village electrification by May 1, 2018.
- The Government of India has sought Parliament's approval for an additional expenditure of Rs 59,978.29 crore (US$ 8.9 billion), which will be used to support the government's rural jobs scheme, building rural infrastructure, urban development and farm insurance.

8.9 RURAL SEGMENT QUICKLY CATCHING UP

- The Fast Moving Consumer Goods (FMCG) sector in rural and semi- urban India is estimated to cross US$ 100 billion by 2025
- The rural FMCG market is anticipated to expand at a CAGR of 17.41 per cent to US$ 100 billion during 2009–25
- Rural FMCG market accounts for 40 per cent of the overall FMCG market in India, in revenue terms
- Amongst the leading retailers, Dabur generates over 40-45 per cent of its domestic revenue from rural sales. HUL rural revenue accounts for 45 per cent of its overall sales while other companies earn 30- 35 per cent of their revenues from rural areas.

8.10 FUTURE ROAD MAP OF RURAL SECTOR

As the trend with urban India, consumers in the rural regions are also expected to embrace online purchases over time and drive consumption digitally. The rural regions are already well covered by basic telecommunication services and are now witnessing increasing penetration of computers and smart phones. Taking advantage of these developments, online portals are being viewed as key channels for companies trying to enter and establish themselves in the rural market. The Internet has become a cost-effective means for a company looking to overcome geographical barriers and broaden its reach.

Market research firm Nielsen expects India's rural FMCG market to reach a size of US$ 100 billion by 2025. Another report by McKinsey Global Institute forecasts the annual real income per household in rural India to rise to 3.6 per cent 2025, from 2.8 per cent in the last 20 years.

8.11 CHECK YOUR PROGRESS

1. The demand for goods in India and services in India depends largely on

A. Agriculture
B. Rainfall
C. Income
D. Inflation

2. Media have a greater effect than the impersonal ones in the rural marketing context?

A. Personal
B. Impersonal
C. Direct
D. Indirect

3. What is the Reason for Corporate Interest in Rural Markets?

A. Untapped potential
B. Unmet needs/low penetration
C. Current consumption a pointer to potential
D. Increasing income and purchasing power
E. All of the above

4. India is a land of agriculture and most of the population resides in

A. Villages
B. Cities
C. Urban town
D. Towns

8.12 SUMMARY

- The rural market of India is fascinating and challenging at the same time. It offers large scope on account of its sheer size and it is growing steadily.
- Even a small growth can push up the sales of a product substantially, in view of the huge base despite the fact that there are enormous amount of problems.
- It is an attractive market from this angle also that the urban market is highly competitive; the rural market is relatively quiet. In fact, for certain products, it is a totally virgin market.
- Successful rural marketing calls for a review of the rural marketing environment, developing proper understanding of the nature and profile of rural consumers, designing the right products to appeal to them, and adopting suitable media as well as appropriate strategies for communication and distribution.
- Rural India is becoming attractive for the brands due to its large size. Urban customers have so many options plus they are very selective over buying things whereas it is comparatively easy to sell something to people living in rural areas of the country if your brand has won the loyalty of customers. There is untapped rural market which has a huge potential.

8.13 KEY WORDS

- **Rural marketing:** Rural marketing is a process of developing, pricing, promoting, and distributing rural specific goods and services leading to desired exchange with rural customers to satisfy their needs and wants, and also to achieve organizational objectives

- **E-retailing:** The sale of goods and services using an electronic B2C platform using the internet.
- **E-trading:** The process of selling and purchasing of financial products over the internet.
- **BOP**: Balance of Payment.
- **MGNREGA** : Mahatma Gandhi National Rural Employment Guarantee Act

8.14 SELF ASSESSMENT TESTS

1. Define rural marketing. How will you add value to rural marketing?

2. How does rural marketing differ from urban marketing?

3. Provide suitable guidelines to companies planning to go rural.

4. If you wish to enter into rural market, how will you access the different factors of environment and why? Elaborate.

5. What is the role of Government in developing infrastructure in rural areas?

8.15 ANSWERS TO CHECK YOUR PROGRESS

1. Agriculture

2. Personal

3. E. All of these

4. Villages

8.16 SUGGESTED/FURTHER READINGS

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Course: Business Environment	
Course Code: **MBA 105**	Author: **Dr. Rajiv Kumar**
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Global Business Environment

STRUCTURE

9.0 Learning Objectives

After going through this lesson, the learners should be able to:

- Distinguish between global and international business.
- Understand the factors affecting global business environment.
- Know the methods of global business environment analysis.
- Understand about PESTLE analysis.

9.1 Introduction

Countries are sovereign states that have definite geographical regions and have distinct cultures, languages and people. The countries are politically organized and are distinct and separate from each other and interact with each other through trade and other activities either on an international level or a global level. The word "global" is an adjective which means "concerning the entire earth and not just one or two regions." It is synonymous to "worldwide" and "universal," and it also means "unlimited, unbounded, general, and comprehensive." In recent years, world economic order has been transformed into one that has a global scope. This means an integration of the economies of the various countries of the world with the intention of increasing material wealth through competition and specialization. When economies go global, there is free trade, migration and technological, political, military, and socio-cultural interaction and sharing between nations. "Global" means "the integration of different nations as a single unit."When a company goes global, it means that they have branches and offices in many countries, and their products are distributed worldwide. They have investments in the different countries where their products are sold. It is not only experienced in economics and trade but also in environmental concerns and other relevant issues.

9.2 Difference Between Global And International Business

- "Global" is a word that is used to refer to issues and concerns of the entire world while "international" is a term that is used to refer to issues and concerns of two or more countries.
- "International" has a smaller scope encompassing only two or more countries while "global" has a much larger scope which includes the whole world.

- Although they are sometimes used in lieu of each other, “global” means “all-encompassing and worldwide” while “international” means “foreign or multinational.”
- Global companies have offices and branches as well as investments in other countries while international companies export their products and import the products of the country with which they have international trade relations but hold no investments in each other’s economies.

9.3 Global Business Environment: Meaning

The global business environment can be defined as the environment in different sovereign countries, with factors exogenous to the home environment of the organization, influencing decision making on resource uses and capabilities. The global business environment can be classified into the external environment and the internal environment. The external environment includes the social, political, economic, regulatory, tax, cultural, legal, and technological environments. To work effectively and efficiently, companies operating internationally must understand the social environment of the host country where having business operations. Today there are thousands of MNCs which operate in many parts of the globe. Such companies should acquaint themselves with the language and culture of the country in which they are operating.

As firms have no control over the external environment, their success depends upon how well they adapt to the external environment. A firm’s ability to design and adjust its internal variables to take advantage of opportunities offered by the external environment, and its ability to control threats posed by the same environment, determine its success. The differences between the foreign landscape and the one with which they’re familiar are often huge and multifaceted. Some are quite obvious, such as differences in language, currency, and everyday habits. But others are subtle, complex, and sometimes even hidden. Success in international business depends on understanding a wide range of cultural, economic, legal, and political differences between countries.

9.4 Factors Affecting Global Business Environment

Businesses are affected by an external environment as much as they are affected by the competitors. Global factors influencing business are legal, political, social, technological and economic. Understanding of these factors is important while developing a business strategy.

a. Social factors – These factors are related to changes in social structures. These factors provide insights into behaviour, tastes, and lifestyles patterns of a population. Buying patterns are greatly influenced by the changes in the structure of the population and in consumer lifestyles. Age, gender, etc all determine the buying patterns and understanding of such changes is critical for developing strategies which are in line with the market situations. In a global environment it is important that business strategies are designed keeping in mind the social and cultural differences that vary from country to country. Consumer religion, language, lifestyle patterns are all important information for successful business management.

b. Legal factors – These factors that influence business strategies are related to changes in government laws and regulations. For a successful business operation it is important that the businesses consider the legal issues involved in a particular situation and should have the capability to anticipate ways in which changes in laws will affect the way they must behave. Laws keep changing over a period of time. From the point of view of business it is important that they are aware of these changes in the areas of consumer protection legislation, environmental legislation, health & safety and employment law etc.

c. Economic factors – These factors involve changes in the global economy. A rise in living standards would ultimately imply an increase in demand for products thereby, providing greater opportunities for businesses to make profits. An economy witnesses fluctuations in economic activities. This would imply that in case of a rise in economic activity the demand of the product will increase and hence the price will increase. In case of reduction in demand the prices will go down. Business strategies should be developed keeping in mind these fluctuations. Other economic changes that affect business include changes in the interest rate, wage rates, and the rate of inflation. In case of low interest rates and increase in demand Businesses will be encouraged to expand and take risks. Therefore, business strategies should have room for such fluctuations.

d. Political factors – This refers to the changes in government and government policies. Political factors greatly influence the operation of business. For example: companies operating in the European Union have to adopt directives and regulations created by the EU. The political arena has a huge influence upon the regulation of businesses, and the spending power of consumers and other businesses. Business must consider the stability of the political environment, government's policy on the economy etc.

e. Technological factors – These factors greatly influence business strategies as they provide opportunities for businesses to adopt new innovations and inventions. This helps the business to reduce costs and develop new products. With the advent of modern communication technologies, technological factors have gained great impetus in the business arena. Huge volumes of information can be securely shared by means of databases thereby enabling vast cost reductions, and improvements in service. Organizations need to consider the latest relevant technological advancements for their business and to stay competitive. Technology helps business to gain competitive advantage, and is a major driver of globalization. While designing the business strategies firms must consider if use of technology will allow the firm to manufacture products and services at a lower cost. Firms can select new modes of distributions with the help of technology. It has become easier for companies to communicate with their customer in any part of the world.

f. Environmental factors

Environment factors such as weather, climate change, temperature etc. affects the business firm and the demand pattern of various goods and services. Increasing environment awareness has made this external environment factor a significant issue to be considered by business firms. Move towards environment friendly products and services also have affected the demand pattern of various goods and services.

9.5 Global Business Environmental Analysis

The analysis of the global environment of a company is called global environmental analysis. This analysis is part of a company's analysis-system, which also comprises various other analyses, like the industry analysis, the market analysis and the analyses of companies, clients and competitors. This system can be divided into a macro and micro level. Except for the global environmental analysis, all other analyses can be found on the micro level. Though, the global environmental analysis describes the macro environment of a company. A company is influenced by its environment. Many environmental factors, especially economical or social factors, play a big role in a company's decisions, because the analysis and the monitoring of those factors reveal chances and risks for the company's business. This environmental framework also gives information about location issues. A company is thereby able to determine its location sites. Furthermore, many other strategic decisions are based on this analysis. In addition, the factors are analyzed to evaluate external business developments. It is finally the task of the management to adapt the firm to its environment or to influence the environment in an adequate way. The latter is mostly the more difficult option. There are different instruments to analyze the company's environment which are going to be explained afterwards.

9.6 PESTLE Analysis

One instrument to analyze the company's external environment is the PEST analysis. PEST stands for political, economical, social and technological factors. Two more factors, the legal and environmental factor are defined within the PESTLE analysis.

To explain these environmental factors, it is necessary to say that most of the factors depend on each other and they change over the years. Consequently, when one factor changes it also affects the others. The equality for every company is the main characteristic of the factors in an environmental analysis. The different environmental factors are covered below:

Political and legal factors: Political and legal factors are here regarded as a unit which refers to framework given by politics. The exists regulatory or legal frameworks which can be binding for regions, nations or on an international basis. The frameworks deal with economical issues or issues concerning the labour market. Subsidies for instance fall in the category of economical issues. According to the degree of support through subsidies, a country can be more or less attractive for a company. With respect to the labour law of a country, it can highly influence location decisions too. If e.g. the dismissal protection in a country is very good, a firm may tend to choose a country with a more flexible hire-and-fire-system. Furthermore, the stability of a political system is a real important aspect for most firms. A social market economy with rights for co-determination, regulations for patents, the company's investment and environment protection are main characteristics for a political stable system.

Economical factors: Economical factors deal with national or international economical developments and have a direct influence on supplier and consumer markets. Examples of economical factors that play a big role are: the GDP, the rate of inflation, interests, the change rate, employment or the situation of money markets. These economical factors influence demand, competition intensity, cost pressure and the will to invest. For instance, if the gross domestic product of a country is fairly low, the demand is in general lower than in countries with a higher GDP.

Social factors: Social factors deal with social issues regarding the values, ideas, opinions and the culture of market participants. Market participants can be employees, customers or suppliers. Through their contact with the company, they influence it due to their opinions. The company needs to follow the market participant's change of value and adapt its strategies. Nowadays, a change of values concerning environmental protection is on the move.

Technological environmental factors: Technological environmental factors are meanwhile of a great importance, especially for industrial companies, which underlie a fast technological change. The increasing speed of technological changes, like in microelectronics or robotics indicates risks chances for a company particularly manufacturing companies are affected of that fast evolution.

Environmental factors: At last, environmental factors are becoming more and more important nowadays. These factors regard natural resources and the basis of human life. Among those, the availability of raw materials and energy is the main topic. As the availability of fossil fuels, like oil or coal, gets worse within the next decades, the dependency on those fuels stays pretty risky. Moreover, to show an ecological responsibility, companies should assess and reduce their ecological damage. Through rare raw materials and increasing pollution, an environmentally friendly management gets spotlighted more and more by the public interest. Consequently, eco-friendly products or technologies can even signify a competitive advantage.

9.7 Methods Of The Global Environmental Analysis

The segmentation according to the six presented factors of the PESTLE analysis is the starting point of the global environmental analysis. The analysis can be done with the help of a checklist that evaluates every criteria of a segment. In this manner, the status of the global environment shall be defined. In general, every segment needs to be worked on systematically to recognize changes. Then, the factors and its impacts can be interpreted right. After the segmentation, the analysis consists of four further steps:

1. Environmental Scanning
2. Environmental Monitoring
3. Environmental Forecasting

4. Environmental Assessment

1. **Environmental scanning**

The first step is called scanning in which every segment is analyzed to find trend indicators. Thus, after having examined the segment, indicators for its development are defined. According to Fahey and Narayanan, scanning reveals 'actual or imminent change because it explicitly focuses on areas that the organization may have previously neglected'. Scanning is also used to detect weak signals in the environment, before these have conflated into a recognizable pattern, which might affect the organization's competitive environment. Scanning can include every material published in the media such as television, newspapers and periodicals. This method of scanning is called media-scanning. Product-scanning includes scanning of products which announce re-emerging consumer behaviour. Looking for global trends on the internet can be defined as online-scanning.

2. Modes of scanning

Four modes of scanning can be distinguished. Francis Joseph Aguilar (1967) differentiates between undirected viewing, conditioned viewing, informal search and formal search. 'Undirected viewing' means reading a variety of publications for no specific purpose with the possible exception of exploration. This mode is the most cost-efficient one but it also offers the most benefits. There are a lot of varied sources and information which means that the potential data are unlimited. Data are imprecise and vague and there are no guidelines which determine where the search should be focused.

Applying 'conditioned viewing' the viewer pays attention to the particular kinds of data and assesses their significance for the organization. The field of information is more or less clearly identified. 'Informal searching' can be defined as actively seeking specific information in a relatively unstructured way. The contrast of informal searching is called 'formal searching'. This proactive mode of scanning contains methodologies for obtaining information for specific purposes.

3. Environmental monitoring

Environmental scanning is only one component of global environmental analysis. After having identified critical trends and potential events have to be monitored. The next step in global environmental analysis is called environmental monitoring. It can be defined as 'the process of repetitive observing for defined purposes, of one or more elements or indicators of the environment according to pre-arranged schedules in space and time, and using comparable methodologies for environmental sensing and data collection'. Through environmental monitoring, data about environmental developments are recorded, followed and interpreted. Out of this, historical development changes that are important for the company can be recognized and evaluated. Additionally, the relevance and the reliability of the data sources are tested. Furthermore, it is checked where prognoses are required.

4. Environmental forecasting

The direction, intensity and speed of environmental trends are explored through environmental forecasting. Especially the search for possible threats is of importance. A prognosis of trends is necessary to get a picture of the future. This is done by adequate methods, like strategic foresight or scenario analysis. Several other methods of forecasting are the following: guessing, rule of thumb, and expert judgment, extrapolation, leading indicators, surveys, time-series models and econometric systems. ‘Guessing' and related methods totally rely on luck. Consequently, it is not generally a useful method. In addition, it is almost impossible to evaluate the uncertainty of a guess in advance. ‘Expert judgment' lacks validation being the only component of forecasting. It is hardly to predict which ‘oracle’ is successful.

'Extrapolation' is effective when tendencies exist. Forecasts are most effective when changes are predicted in tendencies. Prediction in changes in tendencies is likely to miss concerning extrapolative methods. ‘Forecasting based on leading indicators' needs a stable relationship between the variables that lead and the variables that are led. If the reasons for the lead are not clear the indicators may give misleading information.

'Surveys' of businesses can give information about the future. They rely on planning which needs to be realized. Changes in business implicate changes in planning. 'Time-series models' are popular forecasting methods. They describe historical patterns of data and they focus on “measurable uncertainty”.

'Econometric systems' of equations are the main tools of economic forecasting. They consist of equations which attempt to “model” the behaviour of economic groups such as consumers, producers, workers, investors etc. moderated by historical experience. There are several advantages of using formal econometric systems. Economists are able 'to consolidate existing empirical and theoretical knowledge which provide a framework for a progressive research strategy to explain their own failures, as well as provide forecasts and policy advice.'

5. Environmental assessment

In the last step of the global environmental analysis, the results of the previous three steps (Scanning, Monitoring, and Forecasting) are assessed. The discovered environmental trends are reviewed to estimate the probability of their occurrence. Furthermore, they need to be analyzed to evaluate whether they represent a chance or a risk for the company. The dimension of the chances or risks is also of importance. Moreover, a reaction strategy to the occurring risks or chances needs to be defined. This is done with the help of the Issue-Impact-Matrix, an adequate instrument to evaluate and prioritize trends. The forecasted environmental factors are here classified with respect to their probability of occurrence and their impact on the company. According to their classification, they demonstrate a high, medium or low priority for the company. The factors with a high occurrence probability and a high, significant impact on the company have the highest priority. The higher the priority, the faster need to be reacted to avoid risks and to benefit from chances. The environmental assessment represents the last step of the global environmental analysis.

9.8 Check Your Progress

Q1. Which factors affect the global business environment?

(A) Social factors (B) Economic factors

(C) Political factors (D) All of the above

Q2. Which one are the methods of global business environment?

(A) Environmental assessment (B) Environmental Forecasting

(C) Both of the above (D) None of the above

Q3. PESTLE analysis includes:

(A) Political factors (B) Economic factors

(C) Social factors (D) All of the above

9.9 Summary

The global business environment can be defined as the environment in different sovereign countries with factors exogenous to the home environment of the organization, influencing decision making on resource use and capabilities. The global business environment can be classified into the external environment and the internal environment. After analyzing global business environment with different methods and organization can be successful globally.

9.10 Key Words

Global Business Environment: Environment effect worldwide businesses.

PESTLE Analysis: Political, Economic, Social, Technological, Legal and environmental factors analysis.

International Business Environment: Environment of two or more countries.

Social Factors: Values, ideas, opinions and the culture of market participants.

Economic Factors: Economical factors deal with national or international economical developments.

9.11 Self-Assessment Test

Q1. What is global business environment and what is difference between global and business environment?

Q2. Describe the methods of global business environment analysis.

9.12 Answer To Check Your Progress

1. (D), 2. (c), 3. (D)

9.13 Suggested/Further Readings

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Course: Business Environment	
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Opportunities And Challenges For MNC'S In India

STRUCTURE

10.0 Learning Objectives

After going through this lesson, the learner should be able to:

- Know about Multinational corporations and their Objectives.
- Understand the Opportunities and Challenges for MNCs in India.
- Know the problems in Growth of MNCs.
- Understand Current status and Criticisms against MNCs in India.

10.1 Introduction

The dynamics of the business environment fostered by the drastic political changes in the erstwhile communist and socialist countries and the economic liberalisation across the world has enormously expanded the opportunities for the multinational corporations, also known by names such as international corporation, transnational corporation, global corporation (or firm, company or enterprise) etc. The rapidity with which the MNCs are growing is indicated by the fact that while according to the World Investment Report 1997 there were about 45000 MNCs with some 2.8 lakh affiliates, according to the World Investment Report 2010 there were more than one lakh of them with about 9 lack affiliates. Only one-third of these affiliates were in the developed countries. China is host about to 36 per cent of the total number of affiliates. The MNCs account for a significant share of the world's industrial investment, production, employment and trade. Although the multinational corporation took birth in the early 1860s, it was after the Second World War that multinationals have grown rapidly. In the early days, the United States was the home of most of the MNCs. Now, there are a large number of Chinese, Japanese and European multinationals. There has been a fast increase of developing country firms in the Fortune 500. In 2014, China had 95, South Korea 17 and from India 8 companies in the list. MNCs of the US are more focused, i.e., they confine their business to one industry or product category. In fact, several American MNCs which attempted diversification, mostly by the acquisitions route, reverted to focus, after bitter experiences with the diversification. Compared with the US MNCs, most

European companies have a much broader product line. Japanese companies, generally, have product lines that are much too broad. Of the top ten corporation in the US, only one (General Electric) is a classic conglomerate, while in Japan eight are conglomerates and only two are not (Toyota Motor and Nippon Telegraph and Telephone). Similarly, the Korean corporations are far too diversified. Recent trends indicate that the diversified corporations have many odds against them and the focus strategy is more successful.

As the concept of multinationality has several dimensions, there is no single universally agreed definition of the term multinational corporation. According to an ILO Report, "the essential nature of the multinational enterprises lies in the fact that its managerial headquarters are located in one country (referred to for convenience as the ("home country") while the enterprise carries out operations in a number of other countries as well ("host countries"). Obviously, what is meant is "a corporation that controls production facilities in more than one country, such facilities having been acquired through the process of foreign direct investment. Firms that participate in international business, however large they may be, solely by exporting or by licensing technology are not multinational enterprises." Among the various other benchmarks sometimes used to define 'multinationality' is that the company in question must:

- Produce (rather than just distribute) abroad as well as in the headquarters country
- Operate in a certain minimum number of nations (six for example)
- Derive some minimum percentage of its income from foreign operations (e.g., 25 per cent)
- Have a certain minimum ratio of foreign to total number of employees, or of foreign total value of assets
- Possess a management team with geocentric orientations
- Directly control foreign investments (as opposed simply to holding shares in foreign companies).

The definitions of the terms transnational corporation (used to mean the same thing as MNC and similar terms) foreign affiliate, subsidiary and branch given in the UN's World Investment Report are as follows. Transnational Corporations are incorporated or unincorporated enterprises comprising parent enterprises and their foreign affiliates. A parent enterprise is deemed as an enterprise that controls assets of other entities in countries other than its home country, usually by owning a certain equity capital state. An equity capital stake of 10 per cent or more of the ordinary shares or voting power for an incorporated enterprise, or its equivalent for an unincorporated enterprise, is normally considered as a threshold for the control of assets. (In some countries, such as Germany and United Kingdom, the threshold is a stake of 20 per cent or more.) A Foreign Affiliate is an incorporated or unincorporated enterprise in which an investor, who is resident in another economy, owns a stake that permits a lasting interest in the management of that enterprise (an equity stake of 10 per cent for an incorporated enterprise or its equivalent for an unincorporated enterprise). In the World Investment Report, subsidiary enterprise, a subsidiary enterprise, associate enterprise and branches are all referred to as foreign affiliates. A Subsidiary is an incorporated enterprise in the host country in which another entity directly owns more than a half of the shareholders' voting power and has the right to appoint or remove a majority of the members of the administrative, management or supervisory body. An Associate is an incorporated enterprise in the host country in which an investor owns a total of at least 10 per cent, but not more than a half, of the shareholders' voting power.

10.2 Multinational Corporation

This was the type of the corporation popular when many European companies internationalised during the pre-war (1920s and 1930s) when the trade barriers were very high. According to Bartlett and Ghoshal, the multinational organisation is defined by the following characteristics: a decentralised federation of assets and responsibilities, a management process defined by simple financial control systems overlaid on informal personal coordination and a dominant strategic mentality that viewed the company's worldwide operations as a portfolio of national businesses. In a multinational organisation, the decisions, obviously, are decentralised.

10.3 Characteristics Of Multinationals

MNCs will always look out for opportunities. They carry out risk analysis and send their personnel to learn and understand the business climate. They develop expertise understanding the culture, politics, economy and legal aspects of the country that they are planning to enter. The essential element that distinguishes the true multinational is its commitment to manufacturing, marketing, developing R&D, and financing opportunities throughout the world, rather than just thinking of the domestic situation.

Some of characteristics of MNCs are:

(i) Mode of Transfer:

The MNC has considerable freedom in selecting the financial channel through which funds or profits or both are moved, e.g., patents and trademarks can be sold outright or transferred in return through contractual binding on royalty payments. Similarly, the MNC can move profits and cash from one unit to another by adjusting transfer prices on intercompany sales and purchases of goods and services. MNCs can use these various channels, singly or in combination, to transfer funds internationally, depending on the specific circumstances encountered.

(ii) Value for Money:

By shifting profits from high-tax to low-tax nations, MNCs can reduce their global tax payments. In addition, they can transfer funds among their various units, which allow them to circumvent currency controls and other regulations and to tap previously inaccessible investment and financing opportunities.

(iii) Flexibility:

Some to the internationally generated claims require a fixed payment schedule; other can be accelerated or delayed. MNCs can extend trade credit to their other subsidiaries through open account terms, say from 90 to 180 days. This gives a major leverage to financial status. In addition, the timing for payment of fees and royalties may be modified when all parties to the agreement are related.

10.4 Dominance Of MNCs

The global liberalisation has paved the way for fast expansion and growth of the MNCs. The following paragraphs excerpted from the World Investment Reports 2000 and 2003 provide some indications of the economic dominance of the multinationals. Many countries and economic activities are dominated by MNCs, rendering them a formidable force in today's world economy. According to UNCTAD's World Investment Report 2009, there were more than 82,000 multinationals in the world with over 8 lakh foreign affiliates.

The size of large TNCs is sometimes compared to that of countries' economies, as an indicator of the influence that the former have in the world economy. According to one comparison of the sales volume of firms with the GDP of countries, the sales of the top 200 firms accounted for 27.5 per cent of world GDP in 1999. Of the 50 largest "economies", 14 were TNCs and 36 were countries. Their economic impact can be measured in different ways. In 2010, foreign affiliates accounted for about 68 million employees, compared to 21 million in 1990; their sales of almost $33 trillion were more than double the world exports in 2010, compared to 1990 when both were roughly equal; and the stock of outward foreign direct investment (FDD, increased from $1.7 trillion to $6.6 trillion over the same period. Foreign affiliates now account for one-tenth of world GDP and one-third of world exports. Moreover, if the value of worldwide TNC activities associated with non-equity relationships (e.g., international subcontracting, licensing, and contract manufacturers) is considered, TNCs would account for even larger shares in these global aggregates.

10.5 Perspective

Future holds out an enormous scope for the growth of MNCs. The changes in the economic environment in a large number of countries indicate this. For instance, the number of bilateral treaties that promote and/or protect FDI has increased markedly in recent times. A United Nation's Report described several developments that points to a rapidly changing context for economic growth, along with a growing role for transnational corporations in that process. These include:

1. Increasing emphasis on market forces and a growing role for the private sector in nearly all developing countries.

2. Rapidly changing technologies that are transforming the nature of organisation and location of international production.

3. The globalisation of firms and industries.

4. The rise of services to constitute the largest single sector in the world economy; and

5. Regional economic integration, which involve both the world's largest economies as well as selected developing countries.

10.6 Code Of Conduct

It is widely felt that there must be a code of conduct to guide and regulate the MNCs. According to the Brandt Commission, the principal elements of an international regime for investment should include:

1. A framework to allow developing countries as well as transnational corporations to benefit from direct investments on terms contractually agreed upon. Home countries should not restrict investment or the transfer of technology abroad, and should desist from other restrictive practices such as export controls or market, not restrict current transfers such as profits, royalties and dividends, or the repatriation of capital, so long as they are on terms which were agreed when the investment was originally approved or subsequently negotiated.

2. Legislation promoted and coordinated in home and host countries, to regulate the activities of transnational corporations in such matters as ethical behaviour, disclosure of information, restrictive business practices, cartels, anti-competitive

practices and labour standards. International codes and guidelines are a useful step in that direction.

3. Cooperation by Governments in their tax policies to monitor transfer pricing and to eliminate the resort to tax havens.

4. Fiscal and other incentives and policies towards foreign investment to be harmonised among host developing countries, particularly at regional and sub-regional levels, to avoid the undermining of the tax base and competitive positions of host countries.

5. An international procedure for discussions and consultations on measures affecting direct investment and the activities of transnational corporations.

The Code of Conduct for MNCs, drawn up by the Commission on Transnational Corporations, set up by the UN's Economic and Social Council, required MNCs, inter alia, to:

• Respect the national sovereignty of host countries and observe their domestic laws, regulations and administrative practices.

• Adhere to host nations' economic goals, development objectives and socio-cultural values.

• Respect human rights.

• Not interfere in internal political affairs or in inter-governmental relations.

• Not engage in corrupt practices.

• Apply good practice in relation to payment of taxes, abstention from involvement in anti-competitive practices, consumer and environmental protection and the treatment of employees.

• Disclose relevant information to host country governments.

According to the 1976 declaration of the OECD Code of Practice on MNC operations, MNCs should contribute positively to economic and social progress within host nations. Its main provisions were that MNCs should:

- Contribute to host countries' science and technology objectives by permitting the rapid diffusion of technologies.
- Not behave in manners likely to restrict competition by abusing dominant positions or market power.
- Provide full information for tax purposes.
- Consult with employee representatives regarding major changes in operations, avoid unfair discrimination in employment and provide reasonable working conditions.
- Consider the host nation's balance of payments objectives when taking decisions.
- Regularly make public significant information on financial and operational matters, host countries themselves should, the Code insists, possess the absolute right to nationalise foreign-owned assets within their frontiers, but must pay proper compensation. It is very interesting to note that the demands by developing countries that the Code become legally binding were rejected by the UN General Assembly, at the behest of economically advanced countries.

10.7 Opportunities And Challenges For MNCs In India

For succeeding in India, you need to cater the locals with their local flavour, keep your prices competitive, value their diverse cultures, not hurt sentiments, provide outstanding services, and lot more things. India witnessed a number of foreign companies entering India since liberalisation in 1991. Out of these companies, many have shut down in short terms, since they could not survive India. Be it General Motors announcing its exit in mid-2017, or banks like Barclays and Royal Bank of Scotland shutting down their banking services, there were a number of reasons for their failure. Often times, the challenges they faced weren't accounted for in initial planning. Let us dwell deeper into some common challenges Multi-National Companies face while setting up business in India.

1. Infrastructure

Selecting a suitable place in India can be quite a challenge for Multinational Companies. Western companies tend to lease office spaces rather than owning it. Due to lack of professional infrastructure and high demands, companies need to book offices in under construction buildings way before they are completed. Not only this, they also need to lease large office spaces in the very beginning to keep a check on growth of the company, and availability of more space. This creates quite a hassle in the beginning for the spaces are too large for the amount of people it holds. Once the company grows, and there is scope of expansion, a company should be considered lucky if it gets another office near the existing ones. For instance, HP has more than 20 offices in Bangalore which are scattered all over the city. Now, it is looking towards constructing its own office campus, getting into real estate business, which was never in its initial plan.

2. Recruitment

Recruitment is another challenge for the companies as there is an enormous crowd applying for jobs in India, whereas the number of quality and talented professionals is very less. The fact that India has become a hub for IT/Software and Service sector, there is a race among top multinationals to hire the best available talent in the country. Also, the supply of labour is enormous in the country. To filter out the cream is a challenge in itself. For instance, there was once a time when there was a scarcity of software engineers in India, and hence, companies paid them high since the supply was low. Now, the tables have turned completely. Companies like Infosys receive more than 1.4 million applications in a year, out of which not more than 60–70k are interviewed. The final selection is as low as 25,000 per company. Since the supply has skyrocketed, the cost of labour has gone down. It is only a cream of students from top institutes who are employed by such companies.

3. Diverse culture

While Unity in Diversity is one of the top strengths of India, it is also one big weakness for the companies to set up their business. Since most companies are western, and the top management is foreign in the beginning, there is a huge problem in coping up with the culture of the diversity of employees they hire. This can stir quite unrest in the employees. In mono culture teams and countries, a person can freely express his views, whereas, in a diverse cultural nation like India, you are more likely to offend people with your thoughts and opinions.

4. Price centric customers

In India, another problem that companies face is the mentality of the people in buying goods and availing services. India is more of a price centric nation, which does not witness as much brand loyalty, as it does consider the price. Hence, not only do the companies need to provide quality products, they also need to charge a competitive price for that. People would compare features without going into the premium depth, and hence choose a cheaper version. The fall of the telecom sector is a perfect example for the price centric mentality of the people. For well settled companies which entered India are used to these challenges. Whereas, companies who have just started on a multinational path, have a long way to go to understand how the cultural, political and legal system works in India. The suggested solutions for all companies to deal with the government and also with cultural and recruitment problems is to hire Business Consultants or Senior Management who have in-depth knowledge of the same. India is a country that can provide you with vast business opportunities, only if you know how to utilize it the right way.

10.8 Problems From The Growth Of MNCs

Much of the concern about MNCs stems from their size, which can be formidable. MNCs may impose on their host governments to the advantages of their own shareholders and the disadvantages of citizens and shareholders in the country of shareholders in the past. It can be difficult to manage economics in which MNCs have extensive investments. Since MNCs often have ready access to external sources of finance, they can blunt local monetary policy. When the Government wishes to constrain any economic activity, MNCs may nevertheless expand through foreign borrowing.

Similarly, efforts at economic expansion may be frustrated if MNCs move funds abroad in search of advantages elsewhere. Although it is true that any firm can frustrate plans for economic expansion due to integrated financial markets, MNCs are likely to take advantage of any opportunity to gain profits. As we have seen, MNCs can also shift profits to reduce their total 'tax burden by showing larger profits in countries with lower tax rates citizens and shareholders in the country of shareholders in the past.

It can be difficult to manage economics in which MNCs have extensive investments. Since MNCs often have ready access to external sources of finance, they can blunt local monetary policy. When the host Government wishes to constrain any economic activity, MNCs may nevertheless expand through foreign borrowing. Similarly, efforts at economic expansion may be frustrated if MNCs move funds abroad in search of advantages elsewhere. Although it is true that any firm can frustrate plans for economic expansion due to integrated financial markets, MNCs are likely to take advantage of any opportunity to gain profits. As we have seen, MNCs can also shift profits to reduce their total tax burden by showing larger profits in countries with lower tax rates.

10.9 Multinational Corporations In India

MNCs have been operating in India even prior to Independence like Singer, Parry, Philips, Unit- Lever, Proctor and Gamble. They either operated in the form of subsidiaries or entered into collaboration with Indian companies involving sale of technology as well as use of foreign brand names for the final products. The entry of MNCs in India was controlled by existing industrial policy statements, MRTP Act, and FERA. In the pre-reform period the operations of MNCs in India were restricted.

New Industrial Policy 1991 and Multinational corporations:

The New Industrial Policy 1991 removed the restrictions of entry to MNCs through various concessions. The amendment of FERA in 1993 provided further concession to MNCs in India.

At present MNCs in India can—

(i) Increase foreign equity up to 51 percent by remittances in foreign exchange in specified high priority areas. Subsequently MNCs are free to own a majority share in equity in most products.

(ii) Borrow money or accept deposit without the permission of Reserve Bank of India.

(iii) Transfer shares from one non-resident to another non-resident.

(iv) Disinvest equity at market rates on stock exchanges.

(v) Go for 100 percent foreign equity through the automatic route in Specified sectors.

(vi) Deal in immovable properties in India.

(vii) Carry on in India any activity of trading, commercial or industrial except a very small negative list.

Thus, MNCs have been placed at par with Indian Companies and would not be subjected to any special restrictions under FERA.

10.10 Criticisms Against MNCs In India

The operations of MNCs in India have been opposed on the following grounds:

(i) They are interested more on mergers and acquisitions and not on fresh projects.

(ii) They have raised very large part of their financial resources from within the country.

(iii) They supply second hand plant and machinery declared obsolete in their country.

(iv) They are mainly profit oriented and have short term focus on quick profits. National interests and problems are generally ignored.

(v) They use expatriate management and personnel rather than competitive Indian Management.

(vi) Though they collect most of the capital from within the country, they have repatriated huge profits to their mother country.

(vii) They make no effort to adopt an appropriate technology suitable to the needs. Moreover, transfer of technology proves very costly.

(viii) Once an MNC gains foothold in a venture, it tries to increase its holding in order to become a majority shareholder.

(ix) Further, once financial liberalizations are in place and free movement is allowed, MNCs can stabilize the economy.

(x) They prefer to participate in the production of mass consumption and non-essential items.

10.11 Check Your Progress

Multiple choice questions:

1. In order to succeed in Indian market which activity is not major for MNCs.

a. Culture analysis
b. Competitive Price
c. Outstanding services
d. Ambiguous strategies

2. Which of these is the main objective of the MNCs which become a weak point for India?

a. Focus on Mergers and Acquisitions
b. Major eye on short term quick profit
c. Both a and b

d. None of the above

3. ______________a decentralised federation of assets and responsibilities.

a. Liberalisation

b. Multinational Corporation

c. Multilevel companies

d. None of the above

4. Higher growth of MNCs in India can cause:

a. Blunt of monetary policy

b. Advantages to own shareholders

c. Movement of funds outside India

d. All of the above

5. Which of these is not a major challenge or opportunity for MNCs?

a. Infrastructure

b. Finance

c. Diverse culture

d. Recruitment

10.12 Summary

The lesson goes through all aspects of MNCs and their challenges and opportunities in India. *India* has been attracting various *multinational companies* with its attractive and friendly policies. India is an emerging country and the best reason for its development is *MNC's* of *India*. They are multi-process and multi-product enterprises. India is an investment-friendly nation and has attracted the attention of leading multinational organizations because of the population resources, the potential of our workforce, constantly improving when it comes to ease of doing business and a dynamic consumer-oriented market that is quick to absorb new ideas and services.

India benefits from the best multinational companies through their investments, coming in with new technology, contributions to infrastructure, capital and foreign exchange and boosting economic health. Employment generation is also a major aspect. But, at the same time MNC's are facing the challenges to survive and compete in the environment. A MNC always face the challenge of appropriate infrastructure, resources, consumers and many more hurdles to successfully implement their strategies.

Multinational companies are also coming out as a threat for Indian economy as they have their aims which are contradictory to host countries aim. MNCs concentrate on their own short term profits, transferring of funds to their country, recruitment of key personnel from home country and various other aspects. Multinational companies have a long way to go in India and with time it will face new challenges and will get new opportunities.

10.13 Key Words

Multinational Corporation: A *multinational corporation* (*MNC*) is usually a large corporation incorporated in one country which produces or sells goods or services in various countries.

Challenges: MNCs entering a new country face lots of challenges such as availability of resources, infrastructure, labour and various other.

Opportunities: Opportunities are the best prospects available for the MNCs in their host country.

MNCs Growth: MNCs growth in India is causing harm to Indian economy or is boosting the economy is debatable issue.

Code of conduct: They are certain rules or acts to guide the conduct of MNCs.

10.14 Self-Assessment Test

1. What is a Multinational Corporation? What is its nature?
2. What are the major opportunities and challenges faced by MNCs in India?
3. Which are the major threats to Indian economy due to increased rate of MNCs?

4. What is the current status of MNCs in India?
5. "MNCs as Indian economy accelerators or decelerators" Discuss.

10.15 Answer To Check Your Progress

Answer of Multiple Choice Questions

1. d. Ambiguous strategies
2. c. Both a and b
3. b. Multinational Corporation
4. d. All of the above
5. d. Finance

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Foreign Investment In India

STRUCTURE

11.0 Learning Objectives

11.1 Introduction

11.2 Significance Of Foreign Investment

11.3 Type Of Foreign Investments

11.4 Disadvantages In FDIs

11.5 Government **Initiatives To Promote FDI**

11.6 Factors Affecting International Investment

11.7 Growth Of FDIs

11.8 Recent Trends In FDIs

11.9 Check Your Progress

11.10 Summary

11.11 Keywords

11.12 Self-Assessment Test

11.13 Answer To Check Your Progress

11.14 Suggested/References Readings

11.0 Learning Objectives

After going through this lesson, the learner should be able to:

- Know the meaning and significance of Foreign Investment
- Understand the advantages and disadvantages of Foreign Investment
- Know the factors affecting International Investment
- Understand the Growth and Recent Trends in FDIs

11.1 Introduction

Foreign Investment in India

Apart from being a critical driver of economic growth, foreign direct investment (FDI) is a major source of non-debt financial resource for the economic development of India. Foreign companies invest in India to take advantage of relatively lower wages, special investment privileges such as tax exemptions, etc. For a country where foreign investments are being made, it also means achieving technical know-how and generating employment.The Indian government's favourable policy regime and robust business environment have ensured that foreign capital keeps flowing into the country. The government has taken many initiatives in recent years such as relaxing FDI norms across sectors such as defence, PSU oil refineries, telecom, power exchanges, and stock exchanges, among others.

The economic liberalisations that swept across the world, particularly since the late 1980s, have very significantly changed the environment for international investments. At the same time, the surging international capital flows, in its turn, are substantially impacting the business environment. As Peter F. Drucker in his Managing for the Future observers, "increasingly world investment rather than world trade will be driving the international economy. Exchange rates, taxes, and legal rules will become more important than wage rates and tariffs."

11.2 Significance Of Foreign Investment

Following the analysis of Donald MacDougall and Paul Streeten, Gerald Meier observes that, from the standpoint of national economic benefit, the essence of the case for encouraging an inflow of capital is that the increase in real income resulting from the act of investment is greater than the resultant increase in the income of the investor. If the value added to output by the foreign capital is greater than the amount appropriated by the investor, social returns exceed private returns. As long as foreign investment raises productivity, and this increase is not wholly appropriated by the investor, the greater product must be shared with others, and there must be some direct benefits to other income groups as mentioned below:

1. Domestic Labour: Domestic labour may get higher real wages because of the increase in productivity. There might also be an expansion of the employment opportunities.

2. Consumers: If foreign investment is cost-reducing in a particular industry, consumers of the product may gain through lower product prices. If the investment is product-improving or product-innovating, consumers benefit from better quality products or new products.

3. Government: The increase in production and foreign trade resulting from foreign capital might increase the fiscal revenue of the government.

4. External economies: Foreign capital may bring in a number of indirect gains through the realisation of external economies. For instance, if foreign investment is used for the development of infrastructure, this could stimulate domestic investment in industrial and other sectors.

There are various factors that signify the importance of FDI in India some of which are listed below:

1) Helps in balancing international payments:

FDI is the major source of foreign exchange inflow in the country. It offers a supreme benefit to country's external borrowings as the government needs to repay the international debt with the interest over a particular period of time. The inflow of foreign currency in the economy allows the government to generate adequate resources which help to stabilize the BOP (Balance of Payment).

2) FDI boosts development in various fields:

For the development of an economy, it is important to have new technology, proper management and new skills. FDI allows bridging of the technology gap between foreign and domestic firms to boost the scale of production which is beneficial for the betterment of Indian economy. Thus, FDI is also considered an asset to the economy.

3) FDI & Employment:

FDI allows foreign enterprises to establish their business in India. The establishment of these enterprises in the country generates employment opportunities for the people of India. Thus, the government facilitates foreign companies to set up their business entities in the country to empower Indian youth with new and improved skills.

4) FDI encourages export from host country:

Foreign companies carry a broad international marketing network and marketing information which helps in promoting domestic products across the globe. Hence, FDI promotes the export-oriented activities that improve export performance of the country.

Apart from these advantages, FDI helps in creating a competitive environment in the country which leads to higher efficiency and superior products and services.

11.3 Types Of Foreign Investment

Broadly, there are two types of foreign investment, namely, foreign direct investment (FDI) and portfolio investment. FDI refers to investment in a foreign country where the investor retains control over the investment. It typically takes the form of starting a subsidiary, acquiring a stake in an existing firm or starting a joint venture in the foreign country. Direct investment and management of the firms concerned normally go together. If the investor has only a sort of property interest in investing the capital in buying equities, bonds, or other securities abroad, it is referred to as portfolio investment. That is, in the case of portfolio investments, the investor uses his capital in order to get a return on it, but has no much control over the use of the capital.

FDIs are governed by long-term considerations because these investments cannot be easily liquidated. Hence, factors like long-term political stability, government policy, industrial and economic prospects etc. influence the FDI decision, However, portfolio investments, which can be liquidated fairly easily, are influenced by short-term gains. Portfolio investments are generally much more sensitive than FDIs. Direct investors have direct responsibility with the promotion and management of the enterprise. Portfolio investors do not have such direct involvement with the promotion and management. Since the economic liberalisation of 1991, there has been a surge in the FDI and portfolio investments in India. There are mainly two routes of portfolio investments in India, viz., by Foreign Institutional Investors (FIIs) like mutual funds and through Global Depository Receipts (GDRs), American Depository Receipts (ADRs) and Foreign Currency Convertible Bonds (FCCBs). GDRs/ADRs and FCCBs are instruments issued by Indian companies in the foreign markets for mobilising foreign capital by facilitating portfolio investment by foreigners in Indian securities. Since 1992, Indian companies, satisfying certain conditions, are allowed to access foreign capital markets by Euro issues.

11.4 Government Initiatives To Promote FDI

The Indian government has initiated steps to promote FDI as they set an investor-friendly policy where most of the sectors are open for FDI under the automatic route (meaning no need to take prior approval for investment by the Government or the Reserve Bank of India). The FDI policy is reviewed on a continuous basis with the purpose that India remains an investor-friendly and attractive FDI destination. FDI covers various sectors such as Defence, Pharmaceuticals, Asset Reconstruction Companies, Broadcasting, Trading, Civil Aviation, Construction and Retail, etc.

In the Union Budget 2018, the cabinet approved 100% FDI under the automatic route for single-brand retail trading. Under this change, the non-resident entity is permitted to commence retail trading of 'single brand' product in India for a particular brand. Additionally, the Indian government has also permitted 100% FDI for construction sector under the automatic route. Foreign airlines are permitted to invest up to 49% under the approval route in Air India.

The main purpose of these relaxations in foreign investment by the government is to bring international best practices and employee the latest technologies which propel manufacturing sector and employment generation in India. To boost manufacturing sector with a focus on 'Make in India' initiative, the government has allowed manufacturers to sell their products through the medium of wholesale and retail, including e-commerce under the automatic route.

11.5 Disadvantages Of FDI

Foreign capital, private and official (governmental and institutional) have certain limitations. Certain additional risks are associated with the private foreign capital. One of the important limitations to utilise the foreign capital is the absorptive capacity of the recipient country, i.e., the capacity of the country to utilise the foreign capital effectively. Lack of infrastructural facilities, technical know-how, personnel, inputs, market, feasible projects, inefficiency or inadequacy of administrative machinery etc. are important factors that affect the absorptive capacity. Sometimes 'strings' are attached to the official assistance—the recipient country may be pressurised to fall in line with the ideology or direction of the donor.

The following criticisms are levelled against foreign capital:

1. Private foreign capital tends to flow to the high profit areas rather than to the priority sectors.

2. The technologies brought in by the foreign investor may not be adapted to the consumption needs, size of the domestic market, resource availabilities, stage of development of the economy, etc.

3. Through their power and flexibility, the multinational corporations can evade or undermine economic autonomy and control, and their activities may be inimical to the national interests of particular countries.

4. Foreign investment, sometimes, have unfavourable effect on the Balance of Payments of a country because the drain of foreign exchange by way of royalty, dividend, etc., is more than the investment made by the foreign concern.

5. Foreign capital sometimes interferes in the national politics.

6. Foreign investors sometimes engage in unfair and unethical trade practices.

7. Sometimes, foreign investment can result in the dangerous situation of minimising/ eliminating competition and the creation of monopolies or oligopolistic structures.

8. FDI can also potentially displace domestic producers by pre-empting their investment opportunities.

9. Often, several costs are associated with encouraging foreign investment. Meier observes that these costs may arise from special concessions offered by the host country, adverse effects on domestic saving, deterioration in the terms of trade, and problems of balance of payments adjustment.

10. **Other Disadvantages**

- **Disappearance of cottage and small scale industries:** Some of the products produced in cottage and village industries and also under small scale industries had to disappear from the market due to the onslaught of the products coming from FDIs. Example: Multinational soft drinks.

- **Contribution to the pollution:** Foreign direct investments contribute to pollution problem in the country. The developed countries have shifted some of their pollution-borne industries to the developing countries. The major victim is automobile industries. Most of these are shifted to developing countries and thus they have escaped pollution.

- **Exchange crisis:** Foreign Direct Investments are one of the reason for exchange crisis at times. During the year 2000, the Southeast Asian countries experienced currency crisis because of the presence of FDls. With inflation contributed by them, exports have dwindled resulting in heavy fall in the value of domestic currency. As a result of this, the FDIs started withdrawing their capital leading to an exchange crisis. Thus, too much dependence on FDls will create exchange crisis.

- **Cultural erosion:** In all the countries where the FDls have made an inroad, there has been a cultural shock experienced by the local people, adopting a different culture alien to the country. The domestic culture either disappears or suffers a setback. This is felt in the family structure, social setup and erosion in the value system of the people. Importance given to human relations, hither to suffers a setback with the hi-fi style of living.

- **Political corruption:** In order to capture the foreign market, the FDIs have gone to the extent of even corrupting the high officials or the political bosses in various countries. Lockheed scandal of Japan is an example. In certain countries, the FDIs influence the political setup for achieving their personal gains. Most of the Latin American countries have experienced such a problem. Example: Drug trafficking, laundering of money, etc

- **Inflation in the economy:** The presence of FDIs has also contributed to the inflation in the country. They spend lot of money on advertisement and on consumer promotion. This is done at the cost of the consumers and the price is increased. They also form cartels to control the market and exploit the consumer. The biggest world cartel, OPEC is an example of FDI exploiting the consumers.

- **Trade deficit:** The introduction of TRIPs (Trade Related Intellectual Property Rights) and TRIMs (Trade Related Investment Measures) has restricted the production of certain products in other countries. For example, India cannot manufacture certain medicines without paying royalties to the country which has originally invented the medicine. The same thing applies to seeds which are used in agriculture. Thus, the developing countries are made to either import the products or produce them through FDIs at a higher cost. WTO (World Trade Organization) is in favour of FDIs.

- **World Bank and lMF aid:** Some of the developing countries have criticized the World Bank and IMF (International Monetary Fund) in extending assistance. There is a discrimination shown by these international agencies. Only those countries which accommodate FDIs will receive more assistance from these international institutions.

- **Convertibility of currency:** FDIs are insisting on total convertibility of currencies in under-developed countries as a prerequisite for investment. This may not be possible in many countries as there may not be sufficient foreign currency reserve to accommodate convertibility. In the absence of such a facility, it is dangerous to allow the FDIs as they may withdraw their investments the moment they find their investments unprofitable.

11.6 Factors Affecting International Investment

The theories of foreign investment described above have indicated several possible reasons for foreign investment. This section is a further extension of the important factors affecting international investment.

1. Rate of interest: One of the most important stimuli to international capital movements is the difference in the rate of interest prevailing at different places. Capital has a tendency to move from a country with a low rate of interest to a country where it is higher, other things being equal, interest rates or foreign exchange rates.

2. Speculation: Short-term capital movements may be influenced also by speculation pertaining to anticipated changes in the interest rates or foreign exchanges rates.

3. Profitability: Private foreign capital movement is influenced by the profit motive. Hence, other things being equal, private capital will be attracted to countries where the return on investment is comparatively higher.

4. Costs of production: Private capital movements are encouraged by lower costs of production in foreign countries. As Kreinin points out, we may distinguish between two types of cost-reducing investment. The first arises from the need to obtain raw materials from abroad. Such materials may be either unavailable at home or obtainable only at extremely high costs, but they are essential for the production and sale of final products at home or abroad. Without them, profit opportunities would remain unexploited. Indeed, vast investments in the extractive industries are motivated by the fact that the capital must go where the resources are. The second type of cost-reducing investment pertains to costs of commodities other than materials, primarily labour.

5. Economic conditions: Economic conditions, particularly the market potential and infrastructural facilities, influence private foreign investment. The size of the population and the income level of a country have an important bearing on the market opportunities.

6. Government policies: Government policies, particularly towards foreign investment, foreign collaboration, remittances, profits, taxation, foreign exchange control, tariffs, and monetary, fiscal and other incentives, are important factors that may influence foreign investment in a country. Foreign investment can have many undesirable consequences if not properly monitored and regulated.

7. Political factors: Political factors like political stability, nature of important political parties and relations with other countries also influence capital movements.

11.7 Growth Of FDI

Following the sweeping changes in the economic policy, foreign investment has been surging in many countries. Today, the worldwide FDI flows and stocks are about 20 times their size in the early 1980s. Trends in Magnitude of Flows although foreign direct investment flows have their ups and downs; the long-term trend has been one of fast growth. For example, between 1970 and 2000, FDI inflows worldwide increased more than a hundred times. The growth has been the sharpest between 1990 and 2000 thanks to the universal liberalisation, privatisation and the surge in cross-border M&As by these developments. It was estimated at $1461 billion in 2013. After peaking in 2000, the FDI flows had a downturn. The upward trend in inflows began again in 2004. FDI inflows peaked in 2007 ($2100 billion but was lower in subsequent years). While the FDI flows had their ups and downs, the stock of FDI has increased tremendously over time. Worldwide FDI inward stock increased from $1779 billion in 1990 to $5810 in 2000 and further to $11999 billion in 2006. FDI inward stock as a percentage of GDP increased more than four times between 1990 and 2013, from 8.4 per cent to 34.3.

Cyclical Behaviour FDI flows are characterised by cyclical behaviour. The decline in FDI flows after peaking in 2000 followed rapid increases during the late 1990s. As the World Investment Reports point out, there was a similar pattern during the late 1980s and early 1990s, and in 1982- 1983. Thus, this is the third downward cycle in FDI, each punctuating a long upward trend in FDI every ten years or so. Factors Affecting the Trend in FDI Flows The swings in FDI flows reflect changes in several factors. The main ones are business cycles, stock market sentiment and M&As. These short-term factors (including factors such as the terrorist attack of September 11, 2000) work in tandem with longer-term factors, sometimes offsetting and at other times reinforcing them. There is, on the other hand, a stable and positive relationship between global FDI flows and the level and growth of world GDP. Technological change, shrinking economic distance and new management methods favour international production. Their impact is, however, countered by cyclical fluctuations in income and growth. The decline in FDI in 2001 reflected a slowdown in the world economy. More than a dozen countries – including the world's three largest economies fell into recession. On the supply side, FDI is affected by the availability of investible funds from corporate profits or loans, which is in turn affected by domestic economic conditions. On the demand side, growing overseas markets lead TNCs to invest, while depressed markets inhibit them. The more interdependent host and home economies become, and the more widely a recession or upswing spreads, the greater are the corresponding movements in global FDI. Data for 1980-2001 show that a bulge in global FDI accompanies high economic growth, and a trough accompanies low growth. However, the relationship between GDP growth and FDI is not uniform across groups of economies. They go together in developed but not in developing countries. One explanation for the different patterns of FDI flows is that business cycles spread much faster across developed countries than others. A supplementary explanation may be that some countries (as in CEE) had been cut off from substantial FDI flows for so long that they have a lot of "catching up" to do – short-term cycles do not affect their attractiveness. The rise in global FDI flows in 2006 was partly driven by increasing corporate profits worldwide and resulting higher stock prices that raised the value of cross-border mergers and acquisitions (M&As). M&As continued to account for a high share of FDI flows, but greenfield investment also increased, especially in developing and transition economies. As a result of higher corporate profits, reinvested earnings have become an important component of inward FDI. They accounted for an estimated 30 per cent of total inflows worldwide in 2006 and for almost 50 per cent in developing countries alone. One of the important determinants of the FDI trend is the trend in cross-border M&A. For example, the dramatic increases in cross-border M&As led to record flows in 1999 and 2000. Cross-border M&As made its contribution to the decline in the FDI too.

11.8 Recent Trends In FDIs

Enthused by a record foreign investment inflow, India is optimistic of continuing to be one of the world's favourite FDI destinations in 2020 on the back of the Modi government's liberalised norms and a significant jump in the ease of doing business ranking.Secretary in the Department for Promotion of Industry and Internal Trade (DPIIT) GuruprasadMohapatra said that despite a slowdown in the global economy, inflows of foreign investment into the country have not been impacted.India received a USD 27.2-billion foreign investment in the first half of 2019 and the pace is said to have sustained thereafter.The healthy growth in the overseas investments is proving that there is a lot of optimism and enthusiasm about India as a foreign investment destination.All the ministries, departments and states are working to address issues and providing stable policies to facilitate entry of foreign companies. Ease of doing business is very critical for FDI. Foreign companies look into the World Bank's ranking and they have been very impressed with India's much-improved ranking so far. The improvement in the business environment gives a pleasant experience to foreign investors as it helps in making processes easier.Some of the states are also wooing investments. So there is a need to further work on the areas in which the investments are coming and see how quickly and seamlessly, we can give those approvals.

The global companies which are looking to shift their bases from China to India, the government is focusing on those firms which are looking at India as a second investment destination.In the World Bank’s doing business report, India's rank has improved to 63rd this year among 190 economies from 77th last year.The department is also holding a series of meetings to further relax foreign direct investment norms in the coming months in areas like AVGC (animation, visual effects, gaming and comics), and insurance.Although, the FDI is allowed through automatic route in most of the sectors, certain areas such as defence, telecom, media, pharmaceuticals and insurance, government approval is required for foreign investors.Under the government route, the foreign investor has to take prior approval of the respective ministry/department. Through the automatic approval route, the investor just has to inform the RBI after the investment is made.

11.9 Check Your Progress

Multiple Choice Questions:

1. ______________ is a major source of non-debt financial resource for the economic development.

e. Balance of Payment
f. Foreign direct investment
g. GDP
h. None of the above

2. Which of these factors affect the international investment?

e. Economic Conditions
f. Cost of Production
g. Both a and b
h. Only a

3. Which among them is not a disadvantage of FDIs?

e. Exchange crisis
f. Political corruption
g. Cultural erosion
h. Boost to cottage industries

4. Introduction of_________ & _________has restricted the production of certain products in other countries.

e. M&As
f. TRIPs & TRIMs

g. Exchange crisis & Economic Condition

h. FDIs &FIIs

5. Which among these institutions is in favour of FDIs?

e. IMF

f. World Bank

g. World Trade Organisation

h. IDBI

11.10 Summary

Encouraged by the favourable business environment fostered by the global liberalisation, the international private capital flows have been increasing rapidly. Cross-border M&As have been the major driver of the recent surge in the FDI. Foreign capital now contributes a significant share of the domestic investment, employment generation, industrial production and exports in a number of economies, including China. Broadly, there are the following two types of foreign investment;

• Foreign direct investment (FDI) where the investor has control over participation in the management of the firm.

• Portfolio investment where the investor has only a sort of property interest in investing the capital in buying equities, bonds, or other securities abroad. In the case of portfolio investments, the investor uses his capital in order to get a return on it, but has no much control over the use of the capital. The major portfolio investment in the Indian capital market is by the foreign institutional investors (FIIs).

Broadly there are three economic motives of FDI, viz., resources seeking (e.g., exploiting the natural resources of the host country); market seeking (i.e., to exploit the market opportunities of the host countries) and efficiency seeking (like low cost of production deriving from cheap labour). The presence of any (or even all) of these determinants alone need not attract FDI. Several other factors like the political environment, government policies, bureaucratic culture, social climate, infrastructural facilities etc. are also important determinants of FDI. Although the international capital flows to the developing countries have increased substantially in the last one decade or so, they are still predominantly between the developed countries. A small number of countries account for the lion's share of the international capital inflows to the developing world. Although India has substantially liberalised its foreign investment policy, the FDI inflows had been much below the targets. India had not been getting even one-tenth the size of FDI flow to China. Even the cumulative FDI flow to India between 1991 and 2007 was less than the annual flow to China. Bureaucratic problems, certain unfavourable government attitudes, poor infrastructure, labour factors, high input costs etc. are regarded as the major reasons.

11.11 Keywords

1. Foreign Direct Investment: A foreign direct investment (FDI) is an investment made by a firm or individual in one country into business interests located in another country.

2. M&As: Mergers and acquisitions (M&A) is a general term used to describe the consolidation of companies or assets through various types of financial transactions, including mergers, acquisitions, consolidations, tender offers, purchase of assets and management acquisitions.

3. Government Initiatives: The Government takes initiatives to increase FDIs in India as ithasamended FDI policy to increase FDI inflow.

4. Recent Trends: Recent trends mean the recent inflows and outflows of investments which affect the Indian economy.

11.12 Self-Assessment Test

6. What are Foreign Direct Investments and its significance?
7. What are the negative impacts of foreign direct investment for India?

8. Which all factors affect the international investment?
9. What are the recent trends and growth in FDIs?
10. Discuss the government initiatives to enhance FDIs.

11.13 Answers To Check Your Progress

1. b. Foreign Direct Investment

2. c. Both a & b

3. d. Boost to cottage industries

4. b. TRIPs & TRIMs

5. c. World Trade Organisation

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Course: Business Environment	
Course Code: **MBA 105**	Author: **Dr. Rajiv Kumar**
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Indian Foreign Trade And Its Impact On Balance Of Payment

STRUCTURE

12.0 Learning Objectives

After going through this lesson, the learner should be able to:

- Know about the Indian Foreign Trade.

- Understand Foreign Trade Act and Foreign Trade Policy
- Know the Balance of Payment and its Aspects
- Understand the Issues Related to Balance of Payment Situation

12.1 Introduction

The integration of the domestic economy through the twin channels of trade and capital flows has accelerated in the past two decades which in turn led to the India's GDP reaching Rs 190.10 trillion (US$ 2.72 trillion) in 2018-19. Simultaneously, the per capita income also nearly trebled during these years. India's trade and external sector had a significant impact on the GDP growth as well as expansion in per capita income. Provisional estimates of India's GDP during first half of 2019-20 stood at Rs 98.56 trillion (US$ 1.41 trillion).

Total exports from India (Merchandise and Services) registered a growth of 2.13 per cent year-on-year during April 2019-February 2020 to US$ 491.64 billion, while total imports are estimated at US$ 559.45 billion, according to data from the Ministry of Commerce & Industry. The merchandise export stood at Rs 20, 67,408.73crore (US$ 292.91 billion) during April 2019-February 2020 and imports reaching Rs 30, 76,266.13 crore (US$ 436.03 billion) for the same period. The estimated value of services export for April 2019-February 2020 stood at US$ 198.73 billion and import is US$ 123.42 billion. According to Mr Piyush Goyal, Minister for Commerce and Industry, the Government of India is keen to grow exports and provide more jobs for the young, talented, well-educated and even semi-skilled and unskilled workforce of India. The Balance of Payments (BOP) records all economic transactions between residents of a country and the rest of the world. The BOP account mainly consists of the current account and the capital account. The current account includes the transaction of goods, services, primary income, and secondary income between the residents and the rest of the world. The current account balance is largely driven by the movement of goods and services. The capital account comprises credit and debit transactions under non-produced non-financial assets and capital transfers between residents and non-residents. Thus, acquisitions and disposals of non-produced non-financial assets, such as land sold to embassies and sales of leases and licenses, as well as transfers which are capital in nature, are recorded under this account. RBI publishes the balance of payments data every quarter, in two formats, an old format and a BPM6 format as recommended by the IMF. The data has been gathered starting from April-June 1990 from "the handbook of statistics on Indian economy" The time series BPM6 data in the RBI database starts only in April-June 2011, and it is provisional or partially revised, therefore, we have used data as of old format. The overall balance of payment corresponds to the change in reserves. The change in reserves are denoted by opposite signs in the RBI data, i.e. increase in reserves is denoted by (-) sign and decrease in reserves by (+) sign. In our analysis, to make sure that the data is easy to understand we present the change in reserves as (+) if it has increased and (-) if it has decreased.

- **Capital Inflows**

India's foreign exchange reserves were Rs 33.98 lakh crore (US$ 476.09 billion) in the week up to February 14, 2020, according to data from the RBI.

External Sector

In February 2020, Memorandum of Understanding signed between Department of Health and Family Welfare, Government of India and Department of Health and Human Services, Government of the United States of America.

In February 2020, President of Portugal H.E. Mr Marcelo Rebelo de Sousa, Minister of National Defence of Portugal and Minister of State for Shipping(I/C) and Chemical and Fertilizer, Mr Mansukh Mandaviya, signed an Memorandum of Understanding (MOU) to develop a world class National Maritime Heritage Complex at Lothal, Gujarat with the cooperation from the Republic of Portugal.

- In February 2020, cabinet approved the Memorandum of Understanding (MOU) signed between India and Iceland in the field of Sustainable Fisheries Development.
- In January 2020, Memorandum of Understanding (MOU) was signed between India and Finland to improve defence cooperation between Finnish companies and Indian Defence Public Sector Undertakings.
- In January 2020, India signed a Memorandum of Understanding (MOU) with the Department for International Development (DFID-Government of United Kingdom) for facilitating the energy self-sufficiency of the Indian Railways.
- In December 2019, cabinet approved Memorandum of Understanding between Central Electricity Authority, India and Japan Coal Energy Centre, on Japan-India cooperation for Efficiency and Environmental Improvement for Sustainable, Stable and Low-Carbon supply of Electricity.
- The Memorandum of Cooperation (MOC) between Government of India and Government of Japan in order to constitute the 'India-Japan Steel Dialogue' to strengthen cooperation in steel sector got approval from cabinet in December 2019.
- In November 2019, All India Institute of Ayurveda (AIIA) signed a Memorandum of Understanding (MOU) with Western Sydney University, Australia at New Delhi.
- In November 2019, the Memorandum of Understanding (MOU) signed between India and Finland approved by Cabinet in order to strengthen the cooperation in the field of Tourism.
- In October 2019, the Memorandum of Understanding signed between Central Drugs Standard Control Organization (CDSCO) and Saudi Food and Drug Authority in the field of Medical Products Regulation.
- In September 2019, four Memorandum of Understanding (MOUs) were signed between India and Mongolia focusing on cultural exchange protocol, disaster management, space exploration and in field of animal health and dairy.

- In September 2019, Liquefied Natural Gas (LNG) importer Petronet entered into agreement with US LNG developer Tellurian Inc. and invests US$ 2.5 billion.
- In August 2019, four Memorandum of Understanding (MOUs) were signed between India and France focusing on skill development and vocational training, renewable energy, IT services and space research.

12.2 THE FOREIGN TRADE (DEVELOPMENT AND REGULATION) ACT, 1992

This Act which replaced the Imports and Exports (Control) Act, 1947, came into force on 19th June, 1992. No export or import shall be made by any person except in accordance with the provisions of this Act, the orders and rules made under this Act and the export and import policy.

Objective

The objective of the FTDR Act is to provide for the development and regulation of foreign trade by facilitating imports into, and augmenting exports from India and for matters connected therewith or incidental thereto.

The main provisions of the FTDR Act are the following.

1. Development and Regulation: The FTDRA empowers the Central Government to make provision for the development and regulation of foreign trade by facilitating imports and increasing exports.

2. Prohibition and Restriction: The Act also empowers the Central Government to make provision for prohibiting, restricting or otherwise regulating the import or export of goods as and when required. All goods which are so regulated under this sub-section shall be deemed to be goods the import or export of which has been prohibited under section 11 of the Customs Act, 1962, and all the provisions of that Act shall have effect accordingly. It may be noted that it is according to this sub-clause that the Government has provided for negative lists of exports and imports in the EXIM policy.

3. EXIM Policy: The Act lays down that the Central Government may, from time to time, formulate and announce the export and import policy and may also amend that policy.

4. Director General of Foreign Trade: The Act provides for the appointment by the Central Government, of a Director General of Foreign Trade for the purpose of this Act. The DGFT shall advise the Central Government in the formulation of the export and import policy and shall be responsible for carrying out that policy. (The corresponding authority under the Imports and Exports (Control Act), 1947, was called the Chief Controller of Imports and Exports (CCIE)

5. Importer-Exporter Code Number: The Act lays down that no person shall make any import or export except under an Importer-Exporter Code (IEC) Numbers granted by the DGFT or the Officer authorised by him in his behalf. The Director General is empowered to suspend or cancel the Importer-Exporter Code Number granted to any person if there is valid reason to do so, like contravention of law relating to Central excise or customs or foreign exchange or having conducted import/export in a manner gravely prejudicial to the trade relations of India with any foreign country or in a way detrimental to the interests of the country.

6. Issue and Suspension/Cancellation of Licence: The Director General or any other Officer authorised under this Act is empowered to suspend or cancel a licence issued for export or import of good in accordance with this Act for good and sufficient reasons, after giving the licence holder a reasonable opportunity of being heard.

7. Search, Inspection and Seizure: Where any contravention of any condition of the licence of authority under which any goods are imported is suspected or made, any person authorised by the Central Government may search, inspect and seize such goods, documents, things and conveyances subject to such requirements and conditions as may be prescribed.

8. Penalty for Contravention: Where any person makes or abets or attempts to make any export or import in contravention of any provisions of this Act or any rules or

orders made under this Act or the EXIM policy, he shall be liable to a penalty not exceeding one thousand rupees or five times the value of the goods involved, whichever is more.

12.3 FOREIGN TRADE POLICY

Government of India had been announcing Five Year Export-Import Policy (EXIM Policy). Since 2004, it is known as Foreign Trade Policy (FTP). A new Foreign Trade Policy should have come into effect on April 1, 2014 on the expiry of the FTP 2009-14. However, a new Policy was announced only on April 1, 2015, nearly a year after the Narendra Modi Government assumed office, as the new Government needed time to recast the Policy. While unveiling the Policy for 2015-20, Commerce Minister Nirmala Sitharaman stated that it is in line with the initiatives 'Make in India', 'Digital India' and 'Skill India' announced by the government earlier. There will be a mid-term review of the Policy, compared to the past practice of annual reviews. The FTDRA empowers the Central Govt. to take measures for the development and regulation of foreign trade by facilitating imports and promoting exports.

Salient Features: Some of the salient features of the Foreign Trade Policy 2015-20 are outlined below:

- **Objective**

According to the Commerce Minister, the FTP 2015-20 aims at making the country a bigger player in global trade by improving the business environment and simplifying trade transactions in the wake of trade facilitation agreement of the World Trade Organisation. It seeks to provide a stable and sustainable policy environment for foreign trade in merchandise and services and to promote diversification of India's export basket.

- **Export Growth Targets**

The FTP 2015-20 aims at almost doubling the merchandise exports of India from $466 billion in 2013-14 to $900 billion by 2019-20, by raising India's share in world exports from 2 per cent to 3.5 per cent during this period.

- **Simplification and restructuring of reward schemes**

The FTP for 2015-20 has restructured existing incentive schemes and introduced certain new schemes. Earlier, there were 5 different schemes (Focus Product Scheme, Market Linked Focus Product Scheme, Focus Market Scheme, Agri. Infrastructure Incentive Scrip, and VKGUY) for rewarding merchandise exports with different kinds of duty scrip with varying conditions (sector specific or actual user only) attached to their use. Now, all these schemes have been merged into a single scheme, namely Merchandise Export from India Scheme (MEIS) and there would be no conditionality attached to the scrip issued under the scheme. Rewards for eligible export of goods to notified markets under MEIS shall be payable as percentage of realised FOB value (in free foreign exchange). The debits towards basic customs duty in the transferable reward duty credit scrip would also be allowed adjustment as duty drawback. Earlier only the additional duty of customs/excise duty/service tax was allowed adjustment as CENVAT Credit or drawback, as per Department of Revenue rules. The current Policy has replaced the earlier scheme known as Served from India Scheme (SFIS) with Service Exports from India Scheme (SEIS). SEIS shall apply to 'Service Providers located in India' instead of 'Indian Service Providers'. Thus, SEIS provides for rewards to all service providers of notified services, who are providing services from India, regardless of the constitution or profile of the service provider. Incentives under MEIS and SEIS have been extend to units located in SEZs also. For the first time, exports by e-commerce firms will be provided incentives while under the MEIS.

In the Mid-Term Review of the Foreign Trade Policy (FTP) 2015-20 the Ministry of Commerce and Industry has enhanced the scope of Merchandise Exports from India Scheme (MEIS) and Service Exports from India Scheme (SEIS), increased MEIS incentive raised for ready-made garments and made- ups by 2 per cent, raised SEIS incentive by 2 per cent and increased the validity of Duty Credit Scrip's from 18 months to 24 months. In August 2019, Ministry of Commerce plans to introduce new foreign trade policy aimed at providing incentives and guidelines for increasing export in next five financial years 2020-25.

Boost To 'Make In India'

To encourage domestic production, Export Obligation (EO) for domestic procurement under EPCG Scheme has been reduced to 90 per cent of the normal export obligation (6 times at the duty saved amount) to 75 per cent, in order to promote domestic capital goods manufacturing industry. Further, it is proposed to give higher level of rewards to products with high domestic content and value addition, as compared to products with high import content and less value addition. The government also extended tax breaks to exporters of defence, pharma and environment friendly products. The government will focus on branding India's products for which campaigns would be started soon in sectors including pharma and engineering. Traditional exports like handloom alongside yoga in services would also be promoted.

12.4 Balance of Payment

The principal tool for the analysis of the monetary aspects of international trade is the balance of international payments settlement. This statement, also simply known as the 'Balance of Payments' (BOP), is a systematic record of all international economic transactions, visible and invisible, of a country during a given period, usually a year. In other words, the statement is a device for recording all the economy transactions within a given period between the residents of a country and the residents of other countries. The BOP of each of the individual country in technically speaking always 'balances'. Such equality in the debit and credit sides of the BOP, known as equilibrium, has no economic significance. It simply results from the double entry book-keeping procedure which is used to record the transactions.

The analysis of the BOP can be done in terms of its two major sub-divisions: (a) Current Account, and (b) Capital Account.

Current Account

The Current Account can be broken down into two parts, viz., one, balance of trade, and, two, balance on invisibles. The Balance of Trade (BOT) deals only with exports and imports of merchandise (or visible items). The Balance on Invisibles (BOI) shows net receipts on account of invisibles. These include the remittances, net service payments, etc. It is not necessary that the BOT should always balance; more often than not, it will show either a surplus or a deficit on BOI. If the surplus on BOI equals the deficit on BOT, the current account will show a net balance. But then there is no reason why these two balances should always be equal, again, always in opposite directions. As a matter of fact, the balance on current account can always show a deficit or a surplus. A surplus on current account leads to an acquisition of assets or repayment of debts previously contracted, and a deficit involves withdrawal of previously accumulated assets or is met by borrowings.

Capital Account

The capital Account presents transfers of money and other capital items and changes in the country's foreign assets and liabilities resulting from the transactions recorded in the current account. The deficit on the current account and on account of capital transactions can be financed by external assistance (loans and grants) drawing from the International Monetary Fund and allocation of the Special Drawing Rights. The BOP accounts provide a link between the increase in gross external debt and the portfolio and spending decisions of the economy.

Thus, increase in gross external debt = Current account deficit (CAD)

– Direct and long-term portfolio capital inflows

+ Official reserve increases

+ Other private capital outflows

The above equation shows that an increase in external debt can have three broad sources: current account deficits not financed by long-term capital inflows, borrowing to finance a reserve build-up or private outflows of capital.

12.5 Balance Of Payments And Developing Economies

It is well-known in development economics that UDCs invariably start as debtor economies. In the process of development itself, these economies have to import 15 a great deal of capital goods, consumer goods, food and raw materials and spares and components. They also have to import some new technologies and, hence, the total exchange outgo cannot be matched by export earnings. But, it is expected that in a decade or two, as the new capital goods and technologies begin to become effective and their products are directed towards exports, export goods and services become competitive in cost and quality. In that case, the volume of exports expands and, in due course, begins to overtake imports. A developing economy then moves on from being a debtor economy to a balanced one in terms of BOP and, finally becomes a creditor economy, exporting more than it imports and giving credit to buyers. Thus, from being a net debtor in the beginning, it becomes a net creditor in the end and, in fact, begins to invest abroad rather than have others lending to and investing in it.

Current Account Deficit (CAD): Boon or Bane

The general belief is that high CADs are dangerous. In general, this is correct. But the converse – that low CADs are good – is not. As seen above, a CAD is nothing but a measure of a country's saving gap, i.e., the excess of investment over savings. It represents the net transfer of resources from the rest of the world to the country running the deficit. Therefore, in a developing country, with huge needs for funds for investment, a CAD makes sense. It allows it to finance investments that would have been well beyond what it could hope to finance with its own savings. On the flip side, CADs are to be financed by foreign capital inflows. The capital flows are fickle can be reversed, and have to be serviced. The right CAD for any country, therefore, depends on its ability to absorb and service capital inflows. If these resources can be deployed productively and in ways that enhance its ability to repay, a high CAD to GDP ratio is nothing to worry about. But if they cannot, then it is inviting trouble. Too high a ratio can prove unsustainable in the long run as it did in East Asian economies in 1998 and in Mexico earlier. To that extent, low ratio has its advantages. But, very low ratio carries with it an opportunity cost – of not being able to benefit from resources that could be drawn from outside.

12.6 Issues Related To Balance Of Payment Situation

Openness of Indian Economy

As the Table 1 shows, the Indian economy has been steadily becoming more open. If we take the trade measures (rows 2 and 3 in the Table 1) then the Indian economy is more than twice as open as in 1990-91. Similarly, if we take all foreign receipts and payments, on both current and capital accounts, then its ratio to GDP has gone up from 41.9 per cent in the 1990s to 109.3 per cent now. This means, that the total foreign receipts and payments are now more than India's total GDP. This shows the extent of openness of the Indian economy to foreign payments and receipts. What this also means is that monetary and fiscal policy needs to be undertaken very carefully, taking account of possible international effects. As the current problems of Greece and other EU economies shows, no country can now be unmindful of the international consequences of its fiscal deficits. The lesson is not that there cannot be fiscal deficits, but that international consequences need to be kept in mind. Does this make the Indian economy much more vulnerable to the transmission of external shocks, shocks emerging from other parts of the global economy? A brief look at the different impacts of India's own crisis in 1991, the Asian crisis of the late 1990s and the on-going (2007 onwards) global financial crisis will show the differences in impacts, and also the manner in which the Indian economy has been able to withstand these shocks.

1	Openness Indicators (per cent)	Avg. 1990-91 to	Avg. 2003-04 to 2007-08	2010-11

		1999-2000		
2	Exports plus Imports / GDP	18.8	30.4	36.5
3	Exports plus Imports of Goods and Services / GDP	22.9	40.8	49.0
4	Current Receipts and Payments plus Capital Receipts and Payments / GDP	41.9	83.5	109.3

Source: RBI, 2011, Annual Report 2010-11, Appendix Table 1, p. 170.

Does this make the Indian economy much more vulnerable to the transmission of external shocks, shocks emerging from other parts of the global economy? A brief look at the different impacts of India's own crisis in 1991, the Asian crisis of the late 1990s and the on-going (2007 onwards) global financial crisis will show the differences in impacts, and also the manner in which the Indian economy has been able to withstand these shocks.

External Debt

The Indian economy in 1991 was relatively closed, much more so than in the late 1990s or now. Nevertheless, it experienced a severe shock, one which forced a drastic change in trade and even development policy. What was the shock of 1991? India had a negative trade balance, with imports much more than exports. Foreign exchange balances at that time were just below $5 billion, enough to cover just two weeks of imports. At the same time, India had built up large external debts. In order to secure a roll-over of these debt payments, India had to pledge its gold reserves, physically air-lifting some of it to London. It also secured a loan from the IMF to tide over the immediate crisis. How did this external crisis come about? The Indian economy in 1991 was not as open as it is now, yet it faced an external crisis. To understand this crisis, one must turn to the relation between the fiscal deficit and the external deficit. India had a high fiscal deficit, more than 7 per cent of GDP. Its interest rates were high. In national accounting terms an excess of spending over income gets reflected in a balance of payments deficit. This deficit could be covered by foreign investment or debt. But at some point the foreign debt has to be repaid. In the late 1980s a substantial portion of external debt was of the short-term variety. Further, the high government spending behind the fiscal deficit was not used to fund investment — had that been so, and had that resulted in a substantially higher rate of growth, then the economy would have grown and made it possible to service the debt. But the fiscal deficit did not result in greater investment; rather it was used in what is called non-plan (non-investment) expenditure. With that the ratio of debt service to GDP went up and became a multiple of available foreign exchange (see table below). The result was that in 1991 India had reserves that were just sufficient to cover one week's imports. The crisis was averted by borrowing from the IMF and then undertaking reforms of both external and domestic sectors of the economy. The experience of 1991 should not lead to the conclusion that foreign debt must be avoided at all costs. Rather, foreign borrowing is important to increase the volume of funds available for investment in a developing economy. It allows the economy to investment beyond its own savings. But it is also necessary that the borrowed money be used for investment (other than in a situation of a dire emergency, as in a serious drought) so that economy grows and is able to repay the debt. Along with growth, there is a need for foreign earnings too to increase so that the debt can be repaid.

External Shocks

With growing openness of the Indian economy it becomes more susceptible to external shocks. But how open is the Indian economy? There are two measures one can use of openness. One is to take the ratio of exports and imports of goods and services to GDP. This has been rising from about 30.8 per cent in 2002-03 to 46.4 per cent in 2007-08 and now more than 60 per cent in 2009-10.The above measure only deals with trade. But there are also financial inflows on both current and capital accounts. Taking that into account we get a measure of openness (current receipts and gross capital inflows) + (current payments and gross capital flows) as a ratio of GDP. By this measure openness rose from 49 per cent during 1997-98 to 1991-2 to an average of 80 per cent from 2002-03 to 2007-08. The ratio of gross inflows and outflows to GDP was as high as 120 per cent in 2007-08. This second measure better expresses the degree of connections between India and the rest of the world. A country is affected not only by trade flows but also by overall financial flows, on both current and capital accounts. In a completely open economy capital and flow in and out at will. When returns are high compared to other countries, there could be a large inflow. This itself could be destabilising in that there would be an increase in money supply, with the possibility of inflation. On the other side, when returns fall below those in other countries, then there could be a massive outflow of capital, again negatively impacting the economy. India has not followed such a policy of open capital markets. There are controls on both inflows and outflows. This control on capital account used to be criticised in many quarters. But after India better managed the shock from the global economic crisis of 2008-10, there has been appreciation of India's policy of only gradually opening the capital sector. Along with this control on capital flows, India's banking sector too was restrained. It was restricted in the extent to which it could move into non-bank financial sector, such as insurance. Thus, the Indian banking system, unlike those in the developed countries, was not so exposed to the collapse of non-bank sectors such as insurance. Their exposure to banking assets in other countries was also limited.

12.7 Check Your Progress

Multiple Choice Questions:

1. ______________ is a systematic record of all international economic transactions, visible and invisible, of a country during a given period.

i. Balance of Trade

j. Balance of Payment

k. Financial flow

l. None of the above

2. Which act replaced Imports and Exports (Control) Act, 1947?

i. The Foreign Trade Act,1992

j. Planning commission, 1950

k. Both a and b

l. None of the above

3. Which are the issues related to balance of payment.

i. Openness of India economy

j. External shock

k. Both a and b

l. None of the above

4. ______________ is nothing but a measure of a country's saving gap, i.e., the excess of investment over savings.

i. Gross capital Inflow

j. External deficit

k. Current receiving's

l. Current account deficit

5. ______________shows net receipts on account of invisibles.

i. Balance on Invisibles

j. Balance of Trade

k. Both a and b

l. None of the Above

12.8 Summary

India is presently known as one of the most important players in the global economic landscape. Its trade policies, government reforms and inherent economic strengths have attributed to its standing as one of the most sought-after destinations for foreign investments in the world. Also, technological and infrastructural developments being carried out throughout the country augur well for the trade and economic sector in the years to come. Boosted by the forthcoming FTP, India's exports are expected reach US$ 330-340 billion by 2019-20 according to Federation of India Export Organisation (FIEO). Also, with the Government of India striking important deals with the governments of Japan, Australia and China, the external sector is increasing its contribution to the economic development of the country and growth in the global markets. Moreover, by implementing the FTP 2014-19, by 2020, India's share in world trade is expected to double from the present level of three per cent. India has the potential to increase its goods and services exports to Australia to US$ 15 billion by 2025 and US$ 35 billion by 2035. The foreign trade affects the balance of payment, the imports or exports of a country directly affect the current and capital account of the country. There are several issues related to balance of payment situation in India such as openness of the economy, external socks and higher external debts. A country need to see towards all the situations to have a favourable balance of payment.

12.9 Key Words

Foreign Trade: It is the export or import of goods and services between two or more countries.

Foreign Trade Policy: Aims at making the country a bigger player in global trade by improving the business environment and simplifying trade transactions in the wake of trade facilitation agreement of the World Trade Organisation.

Balance of Payment: The principal tool for the analysis of the monetary aspects of international trade is the balance of international payments settlement.

Current Account: The current account records a nation's transactions with the rest of the world specifically its net trade in goods and services, its net earnings on cross-border investments, and its net transfer payments over a defined period of time, such as a year or a quarter.

Capital Account: The capital Account presents transfers of money and other capital items and changes in the country's foreign assets and liabilities resulting from the transactions recorded in the current account.

12.10 Self-Assessment Test

11. What is Foreign Trade and major objectives Foreign Trade Act?
12. Explain the major aspects of Foreign Trade Policy.
13. What is Balance of Payment and its 2 major sub-divisions?
14. How is foreign trade affecting balance of payment?
15. What are the major issues in Balance of payment situation in India?

12.11 Answer To Check Your Progress

Answer of Multiple Choice Questions:

6. b. Balance of payment
7. c. Foreign Trade act,1992
8. c. Both a and b
9. d. Current account deficit
10. a. Balance on Invisibles

12.12 Suggested/ Further Readings

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Course: Business Environment	
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Exchange Rate Movements And India's Competitiveness In The World Economies

STRUCTURE

13.0 Learning Objectives

After going through this lesson, the learner should be able to:

- Know the meaning of foreign exchange rate.
- Understand the History and type of foreign exchange markets.
- Understand Regulation of foreign exchange transaction.
- Know Foreign Exchange Management Act.

13.1 Introduction

Exchange Rate Movement

Foreign exchange market is the market in which foreign currencies are bought and sold. Being a member of IMF, India followed the par value system of pegged exchange rate system. But when the Breton Woods system collapsed in 1971, the rupee was pegged to Pound Sterling for four years after which it was initially linked to the basket of 14 currencies but later reduced to 5 currencies of India's major trading partners. Currently India has adopted the managed exchange rate system. When exchange rates change, you will often hear terms used to describe that change like depreciation, devaluation, appreciation or revaluation. What do these different terms mean? Well they split into two parts. Two of the terms refer to an upward movement of the exchange rate which are explained below:

- **Appreciation** - Describes an upward movement in a freely floating exchange rate. This may occur day by day or perhaps even minute by minute.
- **Revaluation** - This also describes an upward movement in an exchange rate, but in a fixed exchange rate system. This will be a very infrequent event (if ever) and means the government has deliberately changed the fixed value of the exchange rate upwards.

The other two terms are similar, but describe a downward movement in an exchange rate which are:

- **Depreciation** - Describes a downward movement in a floating exchange rate.
- **Devaluation** - This means that the government has changed the fixed rate of a fixed exchange rate downwards.

An appreciation or depreciation in the exchange rate will lead to changes in the relative prices of imports and exports. Depreciation will make exports appear relatively cheaper overseas while imports will be more expensive. Exchange rate is simply value of a currency in terms of another currency. The buyers and sellers of foreign currency include the, brokers, students, commercial banks, central banks, individual firms, foreign exchange brokers etc. The system of exchange rate works through the facility provided by the key players of the markets. The major functions of the foreign exchange include:

I). Transferring currency from one market to other where it is needed in the transactions.

II). Providing short-term credit to the importers, and thereby facilitating the smooth flow of goods and services between the countries.

III). Stabilizing the foreign exchange rate through spot and forward market.

13.2 Historical Background

Since Independence, the exchange rate system in India has transited from a fixed exchange rate regime where the Indian rupee was pegged to the pound sterling on account of historic links with Britain to a basket-peg during the 1970s and 1980s and eventually to the present form of market-determined exchange rate regime since March 1993. The evolution of exchange management is discussed below:

Par Value System (1947-1971): After gaining Independence, India followed the par value system of the IMF whereby the rupee's external par value was fixed at 4.15 grains of fine gold.

Pegged Regime (1971-1992): India pegged its currency to the US dollar (from August 1971 to December 1991) and to the pound sterling (from December 1971 to September 1975).

The Period Since 1991: A two-step downward adjustment of 18-19 per cent in the exchange rate of the Indian rupee was made on July 1 and 3, 1991.

Liberalised Exchange Rate Management System: The Finance Minister announced the liberalised exchange rate management system (LERMS) in the Budget for 1992-93. This system introduced partial convertibility of rupee. Under this system, a dual exchange rate was fixed under which 40 per cent of foreign exchange earnings were to be surrendered at the official exchange rate while the remaining 60 per cent were to be converted at a market-determined rate.

13.3 Kinds Of Foreign Exchange Market In India

A. Spot Market: It refers to a market in which the sale and purchase of foreign currency are settled within two days of the deal. The spot sale and purchase of foreign exchange make the spot market. The rate at which the foreign currency is bought and sold is called spot exchange rate. For all practical purposes, spot rate is treated as the current exchange rate.

B. Forward Market: It refers to that market which deals in the sale and purchase of foreign currency at some future date at a presented exchange rate. When buyers and sellers enter an agreement to buy and sell a foreign currency after 90 days of the deal, it is called forward transaction. The exchange rate settled between buyer and seller for forward sale and purchase of currency is called forward exchange rate.

Types of Exchange Rate Management

A. Fixed Exchange Rate

B. Flexible Exchange Rate

A. The Fixed Exchange Rate

When the exchange rate between the domestic and foreign currencies is fixed by the monetary authority of a country and is not allowed to fluctuate beyond a limit, it is called fixed exchange rate. Under the IMF system, the monetary authority of a member nation fixes the official value of its currency in terms of a reserve currency (usually the US dollar) or a basket of 'key currencies.' The exchange rate so determined is known as currency's par value. It is also called 'pegged' exchange rate.

However, flexibility is allowed within the upper and lower limits prescribed by the IMF, usually 1% up and down, under the normal conditions. The basic purpose of adopting fixed exchange rate system is to ensure stability in foreign trade and capital movements. Under fixed exchange rate system, the government assumes the responsibility of ensuring stability of exchange rate. To this end, the government undertakes to buy and sell the foreign currency-buy when it becomes weaker and sell when it gets stronger. Private sale and purchase of foreign currency is suspended. Any change in the official exchange rate is made by the monetary authority of the country in-consultation with the IMF. In practice, however, most countries adopt a dual system: a fixed exchange rate for all official transactions and a market rate for private transactions.

Arguments in Favour of Fixed Exchange Rate:

First, it provides stability in the markets, certainty about the future course of actions in the Foreign Exchange Market, and it eliminates the risk caused by the uncertainty.

Second, it creates a system for a smooth flow of foreign capital between the nations, as it gives assurance of fixed return on investment.

Third, it removes the possibility of speculative transactions in foreign exchange markets.

Lastly, it reduces the possibility of competitive exchange depreciation or devaluation of currencies.

B. Flexible Exchange Rate

When the exchange rate is decided by the market force (demand and supply of currency), it is called the flexible exchange rate. The advocates of flexible exchange rate have put forward equally convincing arguments in its favour. They have challenged all the arguments against the flexible exchange rate. It is often argued that flexible exchange rate causes destabilization, uncertainty, risk and speculation.

The proponents of the flexible exchange rate have not only rebutted these charges but also have put forward strong arguments in favour of flexible exchange rate.

Arguments in favour of Flexible Exchange Rate:

First, flexible exchange rate provides a good deal of autonomy in respect of domestic policies as it does not require any obligatory constraints. This advantage is of great significance in the formulation of domestic economic policies. **Second**, flexible exchange rate is self-adjusting and therefore it does not devolve on the government to maintain an adequate foreign exchange reserves to stabilize the exchange rate.

Third, since flexible exchange rate is based on a theory, it has a great advantage of predictability and has the merit of automatic adjustment.

Fourth, flexible exchange rate serves as a barometer of actual purchasing power of a currency in the foreign exchange market.

Finally, some economists argue that the most serious charge against the flexible exchange rate, that is, uncertainty, is not tenable because speculative tendency under this system itself creates conditions for certainty and stability. They argue that the degree of uncertainty under flexible exchange rate system, if any, is not greater than one under the fixed exchange rate.

13.4 Regulation Of Foreign Exchange Transactions

Foreign exchange transactions were regulated in India by the Foreign Exchange Regulations Act (FERA), 1973. This Act also sought to regulate certain aspects of the conduct of business outside the country by Indian companies and in India by foreign companies. The FERA was widely described as a draconian and obnoxious law. Following the economic liberalisation ushered in 1991, some amendments to the FERA were effected in 1993. The main objective of FERA, framed against the background of severe foreign exchange problem and the controlled economic regime, was conservation and proper utilisation of the foreign exchange resources of the country. There was a lot demand for a substantial modification of FERA in the light of the ongoing economic liberalisation and improving foreign exchange reserves position. Accordingly, a new Act, the Foreign Exchange Management Act (FEMA), 1999, replaced the FERA.

13.5 Foreign Exchange Management Act

The FEMA, which came into effect from January 1, 2000, extends to the whole of India and also applies to all branches, offices, and agencies outside India, owned or controlled by a person resident in India.

The objectives of FEMA are:

- To facilitate external trade and payments
- To promote the orderly development and maintenance of foreign exchange market.

Dealing in Foreign Exchange:

Section 3 of FEMA imposes restrictions on dealings in foreign exchange and foreign security and payments to and receipts from any person outside India. Accordingly, except as provided in terms of the Act, or with the general or special permission of the Reserve Bank, no person shall—

(a) Deal in any foreign exchange or foreign security with any person other than an authorised person;

(b) Make any payment to or for the credit of any person resident outside India in any manner;

(c) Receive otherwise through an authorised person, any payment by order or on behalf of any person resident outside India in any manner;

(d) Enter into any financial transaction in India as a consideration for or in association with acquisition or creation or transfer of a right to acquire, any asset outside India by any person. Further, same 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.

Holding of Foreign Exchange:

Same 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 Transactions**

FEMA permits dealings in foreign exchange through authorised persons for current account transactions. However, the Central Government can impose reasonable restrictions in public interest.

- **Capital Account Transactions**

Any person may sell or draw foreign exchange to or from an authorised person for a capital account transaction permitted by the Reserve Bank in consultation with the Central Government.

The Reserve Bank may, however, without prejudice to the generality of this, prohibit, restrict or regulate the following:

(a) Transfer or issue of any foreign security by a person resident in India;

(b) Transfer or issue of any security by a person resident outside India;

(c) Transfer or issue of any security or foreign security by any branch, office or agency in India of a person resident outside India;

(d) Any borrowing or lending in foreign exchange in whatever form or by whatever name called;

(e) Any borrowing or lending in rupees in whatever form or by whatever name called between a person resident in India and a person resident outside India;

(f) Deposits between persons resident in India and persons resident outside India;

(g) Export, import or holding of currency or currency notes;

(h) Transfer of immovable property outside India, other than a lease not exceeding five years, by a person resident in India;

(i) Acquisition or transfer of immovable property in India, other than a lease not exceeding five years, by a person resident outside India;

(j) Giving of a guarantee or surety in respect of any debt, obligation or other liability incurred—

1. By a person resident in India and owed to a person resident outside India; or
2. By a person resident outside India.

A person resident in India may hold, own, transfer or invest in foreign currency, foreign security or any immovable property situated outside India if such currency, security or property was acquired, held or owned by such person when he was resident outside India or inherited from a person who was resident outside India. A person resident outside India may hold, own, transfer or invest in Indian currency, security or any immovable property situated in India if such currency, security or property was acquired, held or owned by such person when he was resident in India or inherited from a person who was resident in India. The Reserve Bank may prohibit, restrict, or regulate establishment in India of a branch, office or other place of business by a person resident outside India, for carrying on any activity relating to such branch, office or other place of business. The Reserve Bank shall not impose any restriction on the drawl of foreign exchange for payments due on account of amortisation of loans or for depreciation of direct investments in the ordinary course of business.

Export of Goods and Services

1. Every exporter of goods shall—

(a) Furnish to the Reserve Bank or to such other authority a declaration as specified, containing true and correct material particulars, including the amount representing the full export value or, if the full export value of the goods is not ascertained at the time of export, the value which the exporter, having regard to the prevailing market conditions, expects to receive on the sale of the goods in a market outside India;

(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 the export proceeds by such exporter. For the purpose of ensuring that export value of the goods is received without any delay, the Reserve Bank may direct any exporter to comply with such requirements as it deems fit. Every exporter of services shall furnish to the Reserve Bank or to such other authorities a declaration as specified, containing the true and correct material particulars in relation to payment for such services.

Realisation and Repatriation of Foreign Exchange

Where any amount of foreign exchange is due or has accrued to any person, he shall take all reasonable steps to realise and repatriate it to India within the time and in the manner prescribed by the RBI. Several exemptions are, however, granted to this clause.

- **Contravention and Penalties**

Under this chapter, penalty for any kind of contravention under this Act is liable to a penalty up to thrice the amount involved where it is quantifiable or up to 2 lakh where it is not quantifiable and where such contravention is continuing one, further penalty which may extend to five thousand rupees for every day after the first day during which the contravention continues. This provision is in total contrast to the respective provision in the erstwhile FERA which provided for imprisonment and no limit on fine. Under FEMA, a person will be liable to civil imprisonment only if he does not pay the fine within 90 days from the date of notice and that too after formalities of show cause notice and personal hearing. If he does not respond to the notice, there can be a warrant of arrest.

- **Administration of the Act**

The FEMA has assigned an important role to the Reserve Bank of India in the administration of this Act. The rules, regulations and norms pertaining to several sections of the Act are to be laid down by the RBI in consultation with the Central Government. The Act requires the Central Government to appoint as many officers of the Central Government as Adjudicating Authorities for holding inquiries pertaining to contravention of the Act. There is also a provision for appointing one or more Special Directors (Appeals) to hear appeals against the order of the Adjudicating Authorities. The Central Government shall also establish an Appellate Tribunal for Foreign Exchange to hear appeals against the orders of the Adjudicating Authorities and the Special Director (Appeals). The FEMA provides for the establishment, by the Central Government, of a Director of Enforcement with a Director and such other officers or class of officers as it thinks fit for taking up for investigation the contraventions under this Act.

13.6 FERA And FEMA – A Comparison

Important differences between FERA and FEMA have been summed up as follows:

1. In FEMA, only the specified acts relating to foreign exchange are regulated, while in FERA, anything and everything that has to do with foreign exchange was controlled. Also, the aim of FEMA is facilitating trade as against that of FERA, which was to prevent misuse. In other words, the theme of FERA was: 'everything that is specified is under control'. While the theme of FEMA is: 'everything other than what is expressly covered is not controlled'. Thus there is a lot of deregulation.

2. FEMA is a much smaller enactment - only 49 sections as against 81 of FERA.

3. In the process of simplification, many of the "lay downs" of the erstwhile FERA have been withdrawn.

4. Many provisions of FERA like the ones relating to blocked accounts, Indians taking up employment abroad, employment of foreign technicians in India, contracts

in evasion of the act, vexatious search, culpable mental state etc., have no appearance in FEMA.

13.7 Check Your Progress

Multiple Choice Questions:

6. ______________ regulated the foreign exchange transactions in India and which sought to control certain aspects of the conduct of business outside the country by Indian companies and in India by foreign companies.

a. FERA
b. FEMA
c. Flexible exchange rate
d. None of the above

7. ______________ a market in which the sale and purchase of foreign currency are settled within two days of the deal.

a. Flexible exchange rate
b. Forward market
c. Spot market
d. None of the above

3. ______________this means that the government has changed the fixed rate of a fixed exchange rate downwards.

a. Appreciation
b. Devaluation
c. Revaluation
d. Depreciation

4. Reserve Bank without prejudice to the generality of this prohibits, restrict or regulate the following.

a. Deposits between person's resident in India and persons resident outside India.

b. Export, import or holding of currency or currency notes.
c. Transfer or issue of any security by a person resident outside India.
d. All of the above

5. What are the objectives of FEMA?

a. To promote the orderly development and maintenance of foreign exchange market
b. To facilitate external trade and payments
c. Both a & b
d. Only b

13.8 Summary

The Foreign Exchange Management Act (FEMA), 1999, replaced the Foreign Exchange Regulations Act (FERA), 1973, which regulated the foreign exchange transactions in India and which sought to control certain aspects of the conduct of business outside the country by Indian companies and in India by foreign companies. The FEMA, which came into effect from January 1, 2000, extends to the whole of India and also applies to all branches, offices, and agencies outside India, owned or controlled by a person resident in India. The objectives of FEMA are to facilitate external trade and payments; and to promote the orderly development and maintenance of foreign exchange market. The Reserve Bank of India is assigned an important role in the administration of this Act. The FEMA empowers the Central Government to impose restrictions on dealings in foreign exchange and foreign security and payments to and receipts from any person outside India. The Act imposes restrictions on persons resident in India on acquiring, holding or owning foreign exchange, foreign security and immovable property abroad and on transfer of foreign exchange or security abroad. The FEMA lays down that all dealings in foreign exchange or foreign security and all payments from outside the country to India shall be made only through authorised persons, except with the general or special permission of the Reserve Bank. The Act also prohibits any payment outside India except with the general or special permission of the Reserve Bank. The FEMA permits dealings in foreign exchange through authorised persons for current account transactions. However, the Central Government can impose reasonable restrictions in public interest. Any person may sell or draw foreign exchange to or from an authorised person for a capital account transaction permitted by the Reserve Bank. However, the Act empowers the RBI to impose a number of restrictions on capital account transactions. The FEMA permits a person resident in India to hold, own, transfer or invest in foreign currency, foreign security or any immovable property situated outside India if such currency, security or property was acquired, held or owned by such person when he was resident outside India or inherited from a person who was resident outside India. Also, a person resident outside India may hold, own, transfer or invest in Indian currency, security or any immovable property situated in India if such currency, security or property was acquired, held or owned by such person when he was resident in India or inherited from a person who was resident in India. The Reserve Bank is empowered by this Act to prohibit, restrict, or regulate establishment in India of a branch, office or other place of business by a person resident outside India, for carrying on any activity relating to such branch, office or other place of business. However, the RBI shall not impose any restriction on the drawl of foreign exchange for payments due on account of amortisation of loans or for depreciation of direct investments in the ordinary course of business. The Act requires the exporters to furnish to the Reserve Bank or to such other authority certain details regarding the exports. For the purpose of ensuring that export value of the goods is received without any delay, the Reserve Bank may direct any exporter to comply with such requirements as it deems fit. Where any amount of foreign exchange is due or has accrued to any person, he shall take all reasonable steps to realise and repatriate it to India within the time and in the manner prescribed by the RBI. Several exemptions are, however, granted to this clause.

Under this chapter, penalty for any kind of contravention under this Act is liable to a penalty up to thrice the amount involved where it is quantifiable or up to ` 2 lakh where it is not quantifiable and where such contravention is continuing one, further penalty which may extend to five thousand rupees for every day after the first day during which the contravention continues. This provision is in total contrast to the respective provision in the erstwhile FERA which provided for imprisonment and no limit on fine. Under FEMA, a person will be liable to civil imprisonment only if he does not pay the fine within 90 days from the date of notice and that too after formalities of show cause notice and personal hearing. If he does not respond to the notice, there can be a warrant of arrest. An important difference between FERA and FEMA is that while in FEMA, only the specified acts relating to foreign exchange are regulated, in FERA, anything and everything that has to do with foreign exchange was controlled. Also, the aim of FEMA is facilitating trade as against that of FERA, which was to prevent misuse. In other words, the theme of FERA was: 'everything that is specified is under control'. While the theme of FEMA is: 'everything other than what is expressly covered is not controlled'. Thus, there is a lot of deregulation.

13.9 Key Words

Exchange rate: In finance, an *exchange rate* is the *rate* at which one *currency* will be exchanged for another. It is also regarded as the value of one country's *currency* in relation to another *currency*.

FERA: Foreign Exchange Regulation Act (also known as FERA), was **introduced in the year 1973.** The act came into force, to regulate inflow and outflow of foreign currency, foreign payments, securities and purchase of fixed assets by the foreigners.

Foreign Exchange Market: The foreign exchange market (also known as forex, FX or the currency market) is an over-the-counter (OTC) global marketplace that determines the exchange rate for currencies around the world. Participants are able to buy, sell, exchange and speculate on currencies.

Foreign Exchange Regulation Act: The Foreign Exchange Management Act, 1999 is an Act of the Parliament of India "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".

FEMA: Foreign Exchange Management Act (FEMA), provisions related to foreign exchange have been modified and liberalised so as to simplify foreign trade and payments.

13.10 Self-Assessment Test

16. What is exchange rate movement?
17. Explain the terms a. "Devaluation"
    b. "Depreciation"
    c. "Appreciation"
    d. "Revaluation"
18. Differentiate between FERA and FEMA.
19. Discuss the objectives of Foreign exchange management act.
20. Explain the flexible and fixed exchange rate.

13.11 Answers To Check Your Progress

1. b. FEMA

2. c. Spot market

3. b. Devaluation

4. d. All of above

5. c. Both a & b

13.12 Suggested/Further Readings

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Course: Business Environment	
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World Trade Trends And **Economic Integration**

STRUCTURE

14.0 Learning Objectives

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14.4 World Trade Trends

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14.7 Check Your Progress

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14.0 Learning Objectives

After going through this lesson, the learner should be able to:

- Understand World trade trends and its important aspects

- Know about WTO and its main functions
- Understand Foreign trade policy of India
- Know Economic Integration and its objectives along with advantages and disadvantages.

14.1 Introduction

Trade is a basic economic concept involving the buying and selling of goods and services, with compensation paid by a buyer to a seller, or the exchange of goods or services between parties. Trade can take place within an economy between producers and consumers. World trade allows countries to expand markets for both goods and services that otherwise may not have been available to it. As a result of international trade, the market contains greater competition and therefore, more competitive prices, which brings a cheaper product home to the consumer. Global trade, in theory, allows wealthy countries to use their resources—whether labor, technology, or capital— more efficiently. Because countries are endowed with different assets and natural resources (land, labor, capital, and technology), some countries may produce the same good more efficiently and therefore sell it more cheaply than other countries. If a country cannot efficiently produce an item, it can obtain the item by trading with another country that can. This is known as specialization in international trade. Trades in different countries have certain restrictions as well as some tariffs, which can be issued in a very discriminatory manner for sure. The discrimination is something which depends on community and country discrimination as well. The policy of economic integration is purely commercial, and it takes place in order to make sure that certain trade barriers are reduced in the best way so that some nations can be unified together. The industrial system in the modern times in resting upon the use of certain techniques which are only applicable from an economic point of view if there is a production that is taking place on a proper large scale. This will require the expanding of the markets on one side and also the increase in the purchasing power of the people on the other side. When it comes to defining economic integration, it can be said that it is basically the unification of different economies to produce a larger economy. The industry works at a different pace in the present times, and there are certain techniques which can be used only in case there is a particular economic angle provided to it in the first place. Well, there is no doubt that economic integration is one of the techniques for sure. With the help of economic integration, the markets can be easily expanded in a way to make sure that the purchasing power of the people is increased as well.

14.2 World Trade

World trade also known as global trade or international trade is simply the import and export of goods and services across international boundaries. It refers to the action of buying, selling or exchanging products and services between nations, companies, people and other entities. Goods and services that enter into a country for sale are called imports. Goods and services that leave a country for sale in another country are called exports. For example, a country may import wheat because it doesn't have much arable land, but export oil because it has oil in abundance.

A fundamental concept underlying global trade is the concept of comparative advantage, developed by David Ricardo in the 19th century. In a nutshell, the doctrine of comparative advantage states that a country can produce some goods or services more cheaply than other countries. In technical terms, the country is able to produce a specific good or service at a lower opportunity cost than others. An opportunity cost is the benefit one gives up in making an economic choice. The classic example is guns and butter - domestic investment over defense spending. The more guns you produce, the fewer funds are available to invest in public schools and infrastructure, for example. The more you invest in the domestic economy, the less you can spend on defense.

"The World Trade Organization provides a forum for negotiating agreements aimed at reducing obstacles to international trade and ensuring a level playing field for all, thus contributing to economic growth and development. The WTO also provides a legal and institutional framework for the implementation and monitoring of these agreements, as well as for settling disputes arising from their interpretation and application." - WTO

14.3 World Trade Organization

The WTO was established in 1995. Before 1995, nations across the world came to international accords through a series of agreements – called GATT (General Agreement on Tariffs and Trade) – which were signed in 1949, 1951, 1955, 1960, 1962, 1973 and 1986.The World Trade Organization today has 164 members – 117 of them are either developing nations or separate customs territories.

It is led by a Director General and a Secretariat, who is supported by 700 staff, all located in Geneva. It has an annual budget of $180 million. It is run by its member governments, with all major decisions made by the member states as a whole, either by delegates, ambassadors, or ministers. Ministers meet every two years in Geneva, Switzerland.

The World Trade Organization often referred to by its initials WTO, is a global international organization that deals with the rules of trade between countries, and helps trading nations resolve disputes. The WTO says it is the only global organization that does this. The World Trade Organization says it aims to help producers of goods and services, importers, and exporters conduct their business. It is a forum for governments from across the world to negotiate trade agreements and settle disputes – under a system of trade rules. Essentially, the World Trade Organization is where member nations' governments try to resolve trade problems that they might have with each other.

14.3.0 World Trade Organization Functions:

According to the WTO, its main functions include:

Reducing Barriers to Trade: such as tariffs, quotas and other obstacles, as well as agreeing on rules regarding the conduct of international trade (e.g. product standards, subsidies, anti-dumping, etc.)

- **Enforcing its Rules:** This involves monitoring and administering the application of its agreed rules for trade in goods and services, and well as trade-related intellectual property rights.
- **Ensuring Transparency:** Transparency of bilateral and regional trade agreements, as well as reviewing and monitoring members' trade policies.
- **Settling Disputes:** between member nations regarding the application and interpretation of the agreements.
- **Building Capacity:** of government officials from developing nations, specifically regarding international trade matters.
- **Accession:** approximately thirty countries are not yet members of the World Trade Organization. WTO aims to help them in the process of joining.
- **Publications:** it is also a center of economic research and analysis. The WTO publishes reports and issues bulletins on international trade.
- **Awareness:** explaining to and educating members of the general public about the WTO's mission and activities

14.3.1 Ministerial Conferences of WTO

Ministerial Conferences	Place	Year	Description
MC1	Singapore	1996	Ministers of finance, trade, foreign and agriculture from more than 120 countries participated and the following issues were in discussion. trade and investment trade facilitation

			transparency in government procurement trade and competition These are known as the Singapore Issues.
MC2	Geneva, Switzerland	1998	Discussions on the implementation of Singapore Issues. Further discussions for next round related to Export subsidies, market access, etc.
MC3	Seattle, USA	1999	The Uruguay Round was discussed. Further discussions on agricultural and services mandated at the last Ministerial. The Ministerial Conference ended without a conclusion though.
MC4	Doha, Qatar	2001	The Doha Round was discussed.
MC5	Cancún, Mexico	2003	Discussions on the progress of the Doha Development Agenda and other negotiations from the last Ministerial.
MC6	Hong Kong	2005	Discussions on aiming to conclude the Doha Round by 2006. Adoption of the 'Swiss Formula' to cut down tariffs on non-agricultural goods (NAMA) by both developed and developing countries with different coefficients.
MC7	Geneva, Switzerland	2009	This meeting didn't revolve around the Doha Round. Ministers discussed various other

			ideas for further development. The theme of MC7 was 'The WTO, the Multilateral Trading System and the Current Global Economic Environment'
MC8	Geneva, Switzerland	2011	Discussions on multiple topics for least developed nations and trade policy reviews. WTO approved Montenegro, Russian Federation and Samoa accessions. Doha Round was discussed to make the mandate more effective, operational and precise.
MC9	Bali, Indonesia	2013	The 'Bali Package' was adopted by the WTO that aimed at the following points: Boosting trade in the least developed countries (LDCs) Higher food security provisions for developing countries Streamlining trade The Bali Package is a selection of issues from the broader Doha Round negotiations. Yemen became a part of WTO.
MC10	Nairobi, Kenya	2015	Discussion on agriculture, cotton and issues of LDCs.The Nairobi Package was adopted by WTO that delivered beneficial commitments to WTO's poorest members.

MC11	Buenos Aires, Argentina	2017	Discussions on e-commerce duties, fisheries subsidies and other commitments to negotiations in all sectors.
MC12	Nur-Sultan, Kazakhstan	2020	Will take place in June 2020.

14.3.2 Doha declaration

The Doha Declaration is the November 2001 declaration that came out of the 4th Ministerial Conference of the WTO that took place in Doha, Qatar.

This declaration gives the mandate for negotiations on an array of topics including issues concerning the implementation of the previous agreements.

This is called the Doha Declaration on the TRIPS Agreement and Public Health.

There were disagreements between developed and developing countries.

The major bones of contention were agriculture, non-tariff trade barriers, industrial tariffs, services and trade remedies.

The Bali Ministerial Declaration was achieved in 2013 which is the first agreement under the Doha Round, and also the first unanimous agreement under WTO.

14.3.3 Dispute settlement of the World Trade Organization

- WTO is an international body that also deals in Dispute Settlements.
- The member country will approach the WTO's dispute settlement body when a country fails to comply with WTO rules.
- All the members are encouraged to settle the disputes through consultation or a panel if the consultation fails.
- The constituted panel will circulate the verdict of the dispute settlement amongst WTO members who can decide to reject the ruling.
- If the ruling is approved, the member country that violated the rules must change rules in line with the WTO Agreement.

- In the case of failure to do so, the complaining country and the violating country may determine a mutually-acceptable compensation, failing which; the complaining country may retaliate suitably.
- Indian industry has had to face greater competition in the wake of globalization. But it has successfully completed, as can be inferred from the fact that there has been no particular surge in imports. In fact, as per the provisional data for 2000-01 our non-oil imports declined by 14 per cent while our exports rose by over 20 per cent in the same period. A close watch is also being kept to ensure that Indian industry does not have to face unfair competition from dumped or subsidized imports of other countries.
- As for drug prices, safeguards are provided like compulsory licensing, price controls, and parallel imports which should help address this concern. It must also be recognized that the prices of medicines are influenced by several factors including the level of competition, size of market, purchasing capacity etc.
- The issue of affordable access to treatment for AIDS, which has gathered international attention in recent months, is hopefully a pointer in the right direction. The TRIPS agreement should not be allowed to hinder the efforts of developing countries to provide affordable access to medicines.
- The apex Indian organizations representing various industries are sincerely working towards ensuring a gainful transition with least disadvantage into the global economy. The government also has to strive to improve infrastructure and provide a facilitating environment for inducing acceleration in trade.

14.4 World Trade Trends

1. The CPTPP

Though President Trump withdrew the U.S. from the TPP in January, the remaining 11 countries are working to resurrect the deal as the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). This deal, if signed, would eliminate approximately 95% of tariffs on trade between these countries, who have a combined GDP of over $10 trillion USD. In November, Canada surprised the other 10 countries by declining to sign the agreement, to the surprise of the negotiators and the Canadian international trade community. However, amid efforts to diversify exports beyond the American market, it seems unlikely that Canada will continue to drag its heels on an opportunity to gain preferential access to the Japanese market in particular. Expect any final issues to be resolved and the CPTPP to be signed sometime in 2018.

2. Ongoing, contentious Brexit talks

By December 2017, the UK has completed the first phase of Brexit negotiations with the EU, covering issues such as the Irish border, citizens' rights and financial settlements. The second phase of negotiations will cover the UK's transition period after formally leaving the EU in March 2019. Discussions over the long-term relationship between the UK and EU will be included in phase three. This process was complicated on December 13, when several Conservative British MPs joined the opposition to vote for an amendment requiring British Parliament to debate and vote on any final deal with the EU before it can be approved. The second phase of Brexit negotiations are planned for 2018, and are expected to present few greater challenges than the first phase. The final phase on the long-term relationship between the UK and EU, however, presents several important questions about economic integration and free trade that Britain's politicians and citizens have not yet agreed upon. With two sets of challenging negotiations, and the extra hurdle of parliamentary approval, the odds that talks will drag into the final three months before the UK leaves the EU on March 29, 2019 remain high.

3. Sustainable, Cleantech exports

If you're involved in the clean tech and sustainability sector, 2018 should be a strong year for you. Despite the U.S. withdrawal from the Paris Agreement, global regulations are still trending towards stricter environmental and emissions regulations, requiring businesses to invest in cleaner technology in order to meet those standards. According to EDC President and CEO Benoit Daignault, total global investment in Cleantech has now exceeded $1 trillion and will reach $2.5 trillion by 2020. Canada in particular is placing great emphasis on this industry. The Canadian government promised $1 billion towards clean tech in its 2017 budget for R&D. The Trade Commissioner Service is also hiring 15 new Trade Commissioners to focus specifically on Cleantech.

4. India, Brazil, and New Zealand – the rising stars of global trade

If you're looking for new markets over the next 12 months, Morgan Stanley recommends you take a hard look at India. They argue the country's increased digitization; new tax laws and younger demographics present a bright future, and predict 7.5% GDP growth in 2018. Morgan Stanley also predicts that India will be the world's fastest growing economy over the coming decade. Brazil will also see a quick recession recovery, growing an expected by 3.1% in 2018, according to the Brazilian government. If you're more interested in fully developed markets, Forbes ranked New Zealand second on its 2018 Best Countries for Doing Business rankings, citing its 3.6% economic growth in 2017, among other factors. The country also ranked highly in several categories for ease of doing business, including first in IP rights, bureaucracy/red tape levels surrounding business, and Transparency International's Corruption Perception Index.

5. Meaningful action to reduce oil dependency

As Venezuela continues to suffer through the collapse of its oil-dependent economy, and the U.S. plans to become a net exporter of oil within 10 years, several oil-dependent economies are taking steps to diversify their economies. In Russia, Putin's approval levels are dropping as the economy struggles through lower oil revenues. Despite making fiscal changes to reduce the national budget's dependence on oil revenues, he may push for new measures to improve his chances in the country's 2018 presidential elections. Saudi Arabia has plans to sell about 5% of Saudi

Aramco, the state-owned oil company, through an IPO in 2018 and expects to generate up to $100 billion for the country's Vision 2030 program, designed to shift the Saudi economy away from oil dependency towards tech and entertainment services. Nigeria and Angola, meanwhile, are looking to agriculture to reduce their oil dependency issues. Nigeria, dependent on oil for 70% of government revenues, has launched a new program to increase yam exports to Europe and the U.S., as the country produces 60% of the world's yams. Angola are instead focused on a broader approach to tap into their agricultural potential, which includes producing more cereals, milk, chicken, cassava, and other products.

6. Banks taking on Block Chain

It is practically impossible these days to tune into the business or financial news and not hear a story about the latest block chain or crypto currency development. Block chain technology, allowing multiple players to have access to a live, unalterable digital ledger, offers game-changing possibilities for international trade finance. In 2018 this buzz worthy fintech is moving beyond Silicon Valley start-ups, into the mainstream world of global financial institutions. In March, 2017, we reported on how banks were working to bring the advantages of blockchain technology to their corporate clients. In May, the R3 Consortium, made up of 70 of the world's biggest financial institutions and created to research and develop block chain adoption, announced it had secured its largest ever investment. Then in October 2017, seven major banks partnered with R3 and Finastra to develop a block chain-based marketplace for syndicated loans. On December 6, Amazon joined the block chain party, announcing a partnership with R3 to allow the Corda platform to be the first distributed ledger technology to operate on the Amazon Web Services Platform. What will we see in 2018? Swiss global financial company UBS has led an initiative to create a "utility settlement coin" that would represent each major national currency. If this coin is launched, the Corda platform could be adapted to facilitate its use. IBM is working on launching their own block chain platform that would allow banks to rapidly clear global payment transactions. There are also several start-ups working on digitizing the bill of lading process. 2018 could be the year some of the block chain-based payment initiatives move from development to adoption.

7. Adoption of futuristic Supply Chain Technology

Machine learning, automation and robotics, self-driving vehicles, new tracking technology – all of these futuristic supply chain tools will see major developments and implementation in 2018. The past year was a big one for self-driving vehicles, culminating with the reveal of Tesla's new fully electric semi, gaining pre-orders from big players such as PepsiCo, UPS and Walmart. Companies invested over $1 billion into self-driving and other trucking technologies in 2017. Speaking of investing in supply chain technology, over $4 billion was invested in AI by U.S. venture capitalists in the past year. One application that has seen immediate return for companies adopting machine learning capable AI is Multi-Echelon Inventory Optimization (MEIO), which has been shown to reduce inventories by 30% while maintaining or improving customer fill rates. Robots will also continue to play more of a role in warehouses in 2018. While some are increasingly capable of working independently, replacing human workers on the floor, others are working alongside humans, or being controlled by humans using VR applications. There's no doubt that the demand for the skills needed to work with robotics will continue to rise in the year ahead.

8. Planning for the possibility of a world without NAFTA

The sixth round of NAFTA talks is set to kick off in Montreal January 23. But as the negotiations near, there doesn't seem to be a lot of positivity. The first five rounds reportedly saw very little progress, putting even more pressure on this next round. What's the problem? The U.S. is seemingly immovable on five issues that pose major problems for the agreement's other two member countries, Canada and Mexico. If this really does spell the end of NAFTA, the Canadian auto, pulp and paper, chemicals, mining, aerospace and oil and gas industries are likely to be most affected, according to BMO chief economist Douglas Porter. Even without NAFTA, trade between the three nations is inevitable. How businesses adapt to the realities of a new – or non-existent – NAFTA, is something we'll be watching closely in 2018.

9. Cyber threats and IP risks

As technology gets more sophisticated and ingrained in our work and personal lives, so too does the threat of cyber security breaches, which in turn compromises our intellectual property. Sixty-four percent of companies surveyed reported some experience of web-based attacks in the past year. Companies of all sizes are targeted and face the risk of cyber threats from simply being connected to the internet. And the costs are large – the average cost of a data breach in Canada is a jaw-dropping $6.03M. So what types of threats are growing in 2018? Phishing, social engineering attacks, malicious code, botnets, denial of service attacks and ransom ware are all on the rise. Ransom ware in particular is growing in frequency, attacks rose an alarming 50% in 2016. Demonstrative of the damage a ransome ware attack can cause was the aftermath of the Wanna Cry attack in May 2017. Hundreds of thousands of individuals lost access to their data, compromising intellectual property, private customer information, and disrupting commercial processes. As a business, it has never been more crucial to include cyber security programs directly in your strategy, and engage IT professionals to help cover all aspects of your web-based properties.

10. Demand for global trade skills higher than ever

Despite continuing turmoil and uncertainty on the global political stage, Canadian businesses still hold an optimistic outlook about their export opportunities. According to Export Development Canada's Fall 2017 Survey, the majority of respondents believe that export sales will increase in 2018, citing new opportunities, growing demand, and expansion into new markets as stimulating factors. As more businesses of all sizes get involved in international markets, the demand for talent skilled in global trade processes is also growing.

14.5 Foreign Trade Policy Of India

The current Foreign Trade Policy is for the period 2015 – 2020 announced by the Government of India, Ministry of Commerce and Industry on 01st April 2015. Foreign trade policy needs amendments every five years and aims at developing export capability, improving export performance and structure, encouraging foreign trade, and creating a suitable balance of payments position. It is updated every year on the 31st of March, and the modifications, improvements and new schemes become effective from 1st April each year.

India in 1991, after liberalization, totally lifted all sorts of restrictions from trade for the purpose of improvement in the balance of payment position. A strong need was felt for Indian markets to work globally, and the economy was set free. But in a developing economy, it is not possible to develop industries without the protection of policies. Therefore, later, it was necessary for India to impose a restriction on its economy through trade policies to regulate import and export.

14.5.0 Objectives of the Foreign Trade Policy of India

Trade enables economic growth and national development. The main aim is not the mere earning of foreign exchange, but encouraging greater economic activity. The foreign trade policy of India is based on the following major objectives as follows:

- To enable substantial growth in exports from India and import to India to boost the economy.
- To at least double the percentage share of global merchandise trade conducted within the next five years.
- To improve the balance of payment and trade.
- To act as an effective instrument of economic growth by creating employment opportunities for the citizens; the larger the expansion of trade activities, the more the workforce required.
- To provide for sustainable growth by giving access to essential raw materials for production and other components, consumables and capital goods required for increasing production and providing efficient services.

- To raise the technological capacity for production and cost-effectiveness of industry and services, thereby improving their competitive strength in comparison to other countries, and to encourage the accomplishment of internationally accepted standards of quality.
- To provide buyers or clients with high-quality goods and services at globally competitive rates and quality. 'Canalization'- an important feature of Foreign Trade Policy under which specific class of goods can be imported only by designated agencies.
- Creation of opportunities by engaging in good and ethical practices.
- Accelerating the economy from low-level economic activities to high-level economic activities by making it a globally oriented and vibrant economy
- To derive maximum benefits from expanding the global market and seizing the best opportunities available.
- Making policies that favor ease of doing business and e-governance.
- To allow for hassle-free transactions for both import and export.
- Reducing the interference between the exporters and Directorate General of Foreign Trade by reducing the number of export documents.
- To allow the import of technology and equipment's which may help in achieving better international standards of quality and reduce the cost of production.
- Establishing the Advance Licensing System for imported goods needed for manufacturing various goods for export. An Advance License is issued by the Directorate General of Foreign Trade to allow duty-free import of inputs, which are physically integrated with the export product (making normal allowance for wastage).
- To allow the import of certain goods as listed in the Open General License; a kind of export license which is issued by Government to domestic suppliers.

14.5.1 Advantages

1. Optimal use of natural resources:

Foreign trade helps each country to make optimum use of its natural resources. Each country can concentrate on production of those goods for which its resources are best suited. Wastage of resources is avoided.

2. Availability of all type of goods:

It enables a country to obtain goods, which it cannot produce or which it is not producing due to higher costs, by importing from other countries at lower costs.

3. Specialization:

Foreign trade leads to specialization and encourages production of different good in different countries. Goods can be produced at comparatively low cost due to advantages of division of labour.

4. Advantages of large-scale production:

Due to foreign trade, goods are produced not only for home consumption but for exports to other countries also. Nations of the world can dispose of goods which they have in surplus in the foreign markets. This leads to production at large- scale and the advantages of large-scale production can be obtained by all the countries of the world.

5. Stability in prices:

Foreign trade irons out wild, fluctuations in prices. It equalizes the prices of goods throughout the world (ignoring cost of transportation etc.).

6. Exchange of technical know-how and establishment of new industries:

Underdeveloped countries can establish and develop new industries with the machinery equipment and technical know-how imported from developed countries. This helps in the development of these countries and the economy of the world at large.

7. Increase in efficiency:

Due to the foreign competition the producers in a country attempt to produce better quality of goods and at the minimum possible cost. This increases the efficiency and benefits the consumers all over the world.

8. Development of the means of transport and communications:

Foreign trade requires the best means of transport and communication. For the advantages of foreign trade development in the means of transport and communication is also made possible.

9. International co-operation and understanding:

The people of different countries come in contact with each other. Commercial intercourse amongst nations of the world encourages exchange of ideas and culture. It creates co-operation, understanding and cordial relations amongst various nations.

10. Ability to face natural calamities:

Natural calamities such as drought, floods, famine, earthquake etc., affect the production of a country adversely. Deficiency in the supply of goods at the times of such natural calamities can be met by imports from other countries.

11. Other advantages:

Foreign trade helps in many other ways such as benefits to consumers, international peace and better standard of living.

14.5.2 Disadvantages

The important disadvantages of foreign trade that you might not know are listed below:

1. Impediment in the Development of Home Industries:

Foreign trade has an adverse effect on the development of home industries. It poses a threat to the survival of infant industries at home.

Due to foreign competition and unrestricted imports the upcoming industries in the country may collapse.

2. Economic Dependence:

The underdeveloped countries have to depend upon the developed ones for their economic development. Such reliance often- leads to economic exploitation. For, instance most of the underdeveloped countries in Africa and Asia have been exploited by European countries.

3. Political Dependence:

Foreign trade often encourages subjugation and slavery. It impairs economic independence which endangers political dependence. For example, the Britishers came to India as traders and ultimately ruled over India for a very long time.

4. Mis-utilization of Natural resources:

Excessive exports may exhaust the natural resources of a country in a shorter span of time than it would have been otherwise. This will cause economic downfall of the country in the long run.

5. Import of Harmful Goods:

Import of spurious drugs, Luxury articles, etc. adversely affects the economy and well being of the people.

6. Storage of Goods:

Sometimes the essential commodities required in a country and in short supply are also exported to earn foreign exchange. This results in shortage of these goods at home and cause inflation. For example, India has been exporting sugar to earn foreign exchange; hence the exalting prices of sugar in the country.

7. Danger to Internal Peace:

Foreign trade gives an opportunity to foreign agents to settle down in the country which ultimately endangers its internal peace.

8. World Wars:

Foreign trade breeds rivalries amongst nations due to competition in the foreign markets. This may event fully lead to wars and disturbs world peace.

9. Hardships in times of wars:

Foreign trade promotes lopsided development of a country as only those goods which have comparative cost advantage are produced in a country. During wars or when good relations do not prevail between nations, many hardships may follow.

Summary table of recent Indian Foreign Trade (in billion $):

Year	Export	Import	Trade Deficit
1999	36.3	50.2	-13.9
2000	43.1	60.8	-17.7
2001	42.5	54.5	-12.0
2002	44.5	53.8	-9.3
2003	48.3	61.6	-13.3
2004	57.24	74.15	-16.91
2005	69.18	89.33	-20.15
2006	76.23	113.1	-36.87
2007	112.0	100.9	-11.1
2008	176.4	305.5	-129.1
2009	168.2	274.3	-106.1
2010	201.1	327.0	-125.9

2011	299.4	461.4	-162.0
2012	298.4	500.4	-202.0
2013	313.2	467.5	-154.3
2014	318.2	462.9	-144.7
2015	310.3	447.9	-137.6
2016	262.3	381	-118.7
2017	275.8	384.3	-108.5
2018	303.52	465.58	-162.05
2019	330.07	514.07	-184
2020	314.31	467.19	-152.88

14.6 Economic Integration And Its Important Aspects

Economic integration is an arrangement among nations that typically includes the reduction or elimination of trade barriers and the coordination of monetary and fiscal policies. Economic integration aims to reduce costs for both consumers and producers and to increase trade between the countries involved in the agreement. It sometimes referred to as regional integration as it often occurs among neighboring nations. When regional economies agree on integration, trade barriers fall and economic and political coordination increases. It is a proper commercial policy of reducing the trade barriers in a discriminative way so that the nations can be joined together. A simple process where there is an arrangement between two different or more countries where they combine and then form a particularly larger economic region with the help of the process. There is also a removal of certain discriminations and discontinuities which might exist along the frontiers of the nation. There is a common tariff as well as the trade policies which might work against the countries which are outside the country group.

"The creation of the most desirable structure of international economy, removing artificial hindrances to the optimum operation and introducing deliberately all desirable elements of coordination and unification"— Tinberger

14.6.0 Objectives of economic integration

- Establishment of a free trade area
- Creation of a custom union
- Development of a common market
- Achievement of an economic union
- Strengthen the economy with improved political cooperation
- Establish an international image and gain the benefits of specialization
- Improve the operational efficiency of the enterprises and reduce the cost of trade
- Increase the employment opportunities and the availability of goods and services

14.6.1 Forms/types of economic integration

- Preferential Trade Area

  The areas of Preferential Trade are created when the countries that make up the same geographical region agree on the elimination or reduction of tariff barriers for certain products imported from other members of the zone. This is often the first small step towards the creation of a commercial block. This type of integration can be established bilaterally (two countries) or multilateral (several countries).
- Free Trade Area

  Free trade areas (FTAs) are created when two or more countries in a given region agree to reduce or eliminate trade barriers in all products that come from other members. An example of this is the North Atlantic Free Trade Agreement (NAFTA) signed between the United States, Canada and Mexico.

- Customs union

  The countries that sign customs unions assume the obligation to eliminate tariff barriers. They must also accept the setting of a common (unified) external tariff for non-member countries. To export to countries with a customs union, a single tariff payment must be made for the exported goods. The tariff revenues are shared among the member countries, but the country collecting the tax is left with a small additional part.

- Common Market

  A common market, also called the single market, is a step prior to the establishment of full economic integration. In Europe, this type of integration is officially called "internal market". The common market includes not only the tangible products, but all the goods and services that are produced within the economic area. Goods, services, capital and labor can circulate freely. Tariffs are eliminated completely and non-tariff barriers are reduced or eliminated as well.

- Complete Economic Union

  They are commercial blocks that, apart from having a common market for member countries, adopt a common commercial policy towards non-member countries. However, the signatories are free to apply their own macroeconomic policies. An example of this type of integration is the European Union (EU).

- Monetary Union

  It is considered a fundamental step towards macroeconomic integration, since it allows economies to join more and strengthen their integration. The monetary union implies the adoption of a common monetary policy, which includes a single currency (the euro, for example). There is a single exchange rate also and a central bank with jurisdiction for all member countries, which sets interest rates and regulates the currency.

- Economic and Monetary Union
  This stage is the key to achieve competitive integration. The Economic and Monetary Union implies having a single economic market, establishing a common commercial and monetary policy, and adopting a single currency.
- Full Economic Integration
  When this stage is reached, there is not only a single economic market, but also a common commercial, monetary and fiscal policy, together with a single currency. Interest rates and common taxes are included here, as well as similar benefits for all member countries.

All commercial and economic policies, in general, must be harmonized with the guidelines of the central bank of the community.

14.6.2 Advantages of economic integration

Following are the main advantages of economic integration:

1. Economies of Scale

For the individual countries out there, having the small and internal market, there is a limited capacity in order to expand production. With the help of economic integration, there is an offering of having unrestricted access to the different products which are being produced by the member country. This will also provide a pretty strong inducement in order to expand the production that happens in the country and also it allows the people to completely expand the economies of scale which are present in the country. This is certainly one of the biggest benefits that we can think of. This is the case for the individual countries out there that need to have some internal markets. However, in the case of internal markets, the production cannot be increased, and hence, the goods are limited as well. So, economic integration can be a great help in such cases as it aims to provide some access to the countries who want to unify their production markets so that they can provide more goods to the people in the best way and that too without any trouble or hassle.

2. International Specialization

With the help of economic integration, the member countries will be able to have a bigger degree when it comes to the specialization in the processes and the products which are produced in the country. The specialization is completely based on the different advantages of the cost comparison and that too by a particular geographical location. This is also a very good point when we talk about the benefits that the process of integration can provide the countries which are the members in the best way. So, there is no doubt that production for some of the member countries will be increased with the help of economic integration.

3. Qualitative Improvement in Output

There is regional cooperation in the economics of the different countries which can actually lead to several fast changes in the technological aspects and that too in a larger and more efficient scale as well. This can also ease the capital movements for the country too. If there are such amazing and favorable conditions in the member countries, there can be a very good improvement in the qualitative production which can create better chances of growth for the countries. Also, the effects will be in a more efficient and faster scale. In such a case, the capital movement in the countries can be improved in the best way with the help of this technique of economic integration.

4. Expansion of Employment

There are many different countries in the economic integration process, and as these countries organize themselves into the regional economic groups, there will be an unrestricted flow when it comes to the labour of the country and the region as well. With the different countries practicing economic integration in the best way, there is no doubt that it will increase some employment opportunities due to the increase in the labour requirements for sure. So, there will definitely be an increase in the employment opportunities for the people in the country. This will also lead to an increase in income, as well.

All of these changes will lead to a better economy, which is certainly one of the best things that can come out of economic integration. Hence, people will have new chances to get jobs in countries that tend to practice economic integration in the best way. That is one of the main reasons why it is so popular amongst the countries these days. There will be more jobs in the production sector of the countries as well.

5. Trade Improvement

Here we have another benefit that might come from economic integration, and that is definitely one of the best ones for sure. With the help of this process, there will be an increase in the power of bargaining that the member countries might have with the world. This is also responsible for bringing certain improvements when it comes to trade. As there will be more power for the economic member countries, there is simply not a single speck of doubt about the fact that they will be able to have authority when it comes to the trade between the countries.

6. Economic Efficiency

There will be more and more competition within the different member countries which are situated in the region. That is all thanks to the economic integration which happens between the countries. With the help of this process, there will be betterment in the economic efficiency that happens in a particular group, which is certainly very beneficial to the member countries as well.

7. Efficient use of Resources

The first and foremost benefit of economic integration is that it leads to efficient use of resources because when many countries are involved it leads to economies of scale not only in production side but also on the administration side which in turn leads to saving of money, energy and time of all the member nations of the group.

8. Good for Producers as well as Consumers

It is good for producers as well as consumers because producers can sell their products without worrying about trade barriers besides due to the market getting expanded producers can benefit by selling their produce to a larger number of consumers. As far as consumers are concerned they too benefit because producers, in order to cater to a large market, expand their production which in turn leads to economies of scale and eventually it is the consumers who benefit as they get the product at cheaper rates.

9. Progress in trade

All countries that follow economic integration have extremely wide assortment of goods and services from which they can choose. Introduction of economic integration helps in acquiring goods and services at much low costs. This is because the removal of trade barriers reduces or removes the tariffs entirely. Reduced duties and lowered prices save a lot of spare money with countries which can be used for buying more products and services.

10. Ease of agreement

When countries enter into regional integration, they easily get into agreements and stick to them for long periods of time.

11. Improved political cooperation

Countries entering economic integration form groups and have greater political influence as compared to influence created by a single nation. Integration is a vital strategy for addressing the effects of political instability and human conflicts that might affect a region.

12. Beneficial for financial markets

Economic integration is extremely beneficial for financial markets as it eases firm to borrow finances at low rate if interest. This is because capital liquidity of larger capital market increases and the resultant diversification effect reduces the risks associated with high investment.

13. Increase in Foreign Direct Investments

Economic integration helps to increase the amount of money in Foreign Direct Investment (FDI). Once firms start FDI, through new operations or by merger, takeover, and acquisition, it becomes an international enterprise.

14.6.3 Disadvantages of economic integration

Following are the main disadvantages of economic integration

1. Trade Diversion

Because of trade barriers, trade is diverted from a non-member country to a member country despite the inefficiency in cost. For example, a country has to stop trading with a low cost manufacture in a non-member country and trade with a manufacturer in a member country which has a higher cost.

2. National Sovereignty

It requires member countries to give up some degree of control over key policies like trade, monetary and fiscal policies. The higher the level of integration, the greater the degree of controls that needs to be given up particularly in the case of a political union economic integration which requires nations to give up a high degree of sovereignty.

3. Non Members Countries are Sidelined

The biggest disadvantage of this integration is that countries which are not part of the group are sidelined as member countries trade between themselves and ignores the other nations which in a way is an injustice to those nations.

4. Ignoring of Profitable Opportunities

Due to economic integrations countries sometimes are forced to produce and sell for member nations only even if it is less profitable for them which in an economic sense is not a good thing as far as companies are concerned because their prime motive is to earn highest possible profits which in case of this integration is not possible. Hence for example, if companies are getting cheap labor from non-members countries or they are getting a higher price for their product if they sell to non-members countries than they will not be able to do it because of economic integration.

5. Bullying Risk

In case of economic integration, not all countries are the same and due to this chances of bullying of weaker or smaller countries by strong or big countries are there which puts smaller or weaker nations at disadvantage. In simple words, this integration may put some countries to disadvantage due to their size of the economy and due to it, these countries may find terms of economic integration to be harsh to them leading to dissatisfaction among the government of the country as well as citizens of the country.

As one can see from the above pros and cons of economic integration that it is a very complex system and that is the reason why in real life there are only a few examples of successful economic integration as this type of integration requires strong political will as well as teamwork which we all know that not many nations can do.

14.7 Check Your Progress

Multiple choice questions:

1. ________ refers to the action of buying, selling or exchanging products and services between nations, companies, people and other entities.

a) World trade

b) Block chain

c) Custom union

d) None of the above

2. WTO was established in ________.

a) 1980

b) 1985

c) 1995

d) 1990

3. An arrangement among nations that typically includes the reduction or elimination of trade barriers and the coordination of monetary and fiscal policy known as ___________.

a) Economic integration

b) Economic efficiency

c) Monetary trade

d) None of the above

4. Which of the following is the aim of economic integration?

a) Establishment of a free trade area

b) Development of a common market

c) Achievement of an economic union

d) All of the above

5. Which of the following is the type of economic integration?

a) Free trade area

b) Preferential trade area

c) Customs union

d) All of the above

14.8 Summary

This chapter explains the concept of world trade and economic integration and the important aspects related to it. It represents the importance of world trade and economic integration and its contribution in a country growth rate. India's ability to achieve rapid, sustainable development will have profound implications for the world. Trade is a basic economic concept involving the buying and selling of goods and services, with compensation paid by a buyer to a seller, or the exchange of goods or services between parties. Trade can take place within an economy between producers and consumers. World trade allows countries to expand markets for both goods and services that otherwise may not have been available to it. As a result of international trade, the market contains greater competition and therefore, more competitive prices, which brings a cheaper product home to the consumer. Global trade, in theory, allows wealthy countries to use their resources—whether labor, technology, or capital— more efficiently. Because countries are endowed with different assets and natural resources (land, labor, capital, and technology), some countries may produce the same good more efficiently and therefore sell it more cheaply than other countries. If a country cannot efficiently produce an item, it can obtain the item by trading with another country that can. This is known as specialization in international trade.

World trade and economic integration aims to reduce costs for both consumers and producers and to increase trade between the countries involved in the agreement. When regional economies agree on integration, trade barriers fall and economic and political coordination increases. There is a common tariff as well as the trade policies which might work against the countries which are outside the country group. With the help of economic integration, there is an offering of having unrestricted access to the different products which are being produced by the member country. With the help of economic integration, the member countries will be able to have a bigger degree when it comes to the specialization in the processes and the products which are produced in the country. There are many different countries in the economic integration process, and as these countries organize themselves into the regional economic groups, there will be an unrestricted flow when it comes to the labour of the country and the region as well. All countries that follow economic integration have extremely wide assortment of goods and services from which they can choose.

In case of world trade and economic integration, not all countries are the same and due to this chances of bullying of weaker or smaller countries by strong or big countries are there which puts smaller or weaker nations at disadvantage. In simple words, this may put some countries to disadvantage due to their size of the economy and due to it, these countries may find terms of international trade and economic integration to be harsh to them leading to dissatisfaction among the government of the country as well as citizens of the country.

14.9 Key Words

World trade trends, WTO, Economic integration, Free trade area, Common market

14.10 Self Assessment Test

1. Explain the functions of World Trade Organization?

2. What do you mean by world trade? Explain the important aspects of WTO?

3. Explain the term economic integration? What are its main objectives?

4. What do you mean by economic integration? What are advantages and disadvantages of economic integration?

5. Discuss the different types of economic integration?

14.11 Answer To Check Your Progress

Answer of multiple choice questions:

1. a. World trade

2. c. 1995

3. a. Economic integration

4. d. All of the above

5. d. All of the above

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Course: Business Environment	
Course Code: **MBA 105**	Author: **Dr. Rajiv Kumar**
Lesson No. **15**	Vetter: **Dr. Suresh K. Mittal**

Contemporary Issues: Climate Change, Food security, Geopolitics, Sustainable Development And De- Globalization

STRUCTURE

15.0 Learning Objectives

After learning this lesson, the learner should be able to:

- Know the meaning and impact of Climate Change
- Understand issues related to Food security
- Know the meaning and issues of Geopolitics
- Understand about Sustainable Development
- Know about De-Globalisation

15.1 Introduction

Contemporary marketing issues arise out of radically changing worldwide economies. This has significantly transformed ways of marketing. As contemporary marketing issues are rising traditional marketing strategies find unfit to the new framework and consequently companies are required to come up with novel ideas for synergetic interaction with existing and potential customers. As the marketing knowledge is expanding accompanied with vast changes, modern buyers, are now more informed, more demanding and want value creation with marketers. Moreover, Environmental, political, technological, Geographical and socio-cultural changes, further necessitate paradigmatic shift in marketing practices. As we witness the emerging concept of manipulative marketing in response to changing consumer behaviour and their buying pattern.

Contemporary Issues in Marketing are inclusive and eclectic in nature. Innovative marketing people can accord with the new wave and they need to serve as avant garde (ideas and methods) to artistically reciprocate to the changing international political, economic and social scenario.

Contemporary marketing concept is dynamic in the speedily changing marketing technology, environment, social, political, economic and hence marketers have mould the ways of producing, pricing, placing and promoting goods and services. Marketers have to start from the scratch and rethink of segmenting, targeting and positioning strategies in accord with the emerging issues in the surrounding. It is only then marketing world successfully strives to get through the cut throat competition to position their products or services into the minds of customers.

Survival of the fittest

Those marketers who would foresee the changes in existing and upcoming environmental forces would survive in the fray. No business exist in vacuum, it does affect and is also significantly affected by happenings around the world. The marketers who rightly observe the immediate and outside environment, strategise the marketing efforts will survive in the business world. Here in this chapter we will try to understand the contemporary issues rising and to what extent they are affecting the marketing world.

15.2 Contemporary Issue – Climate Change

15.2.1 Introduction of climate change

Climate change is one of the greatest challenges facing the international community. Mitigating global warming and adapting to its consequences will require major economic investment and, above all, unequivocal determination on the part of policy-makers. The long-term impacts of climate changes have been, temperature and sea level rises, and spike in extreme weather events, like wildfires and tropical storms, are critically affecting infrastructure, crop production, and the livability of many heavily populated areas. Climate-related risks are also amplifying growing tensions stemming from trade, geopolitical, and domestic conflicts. Polar ice is melting quickly than expected with significant implications for sea-level rise and emerging geopolitical risk as neighboring states in the Arctic compete for new shipping lanes and natural resources. A growing proportion of the world's population is now more prone to flood due to the dual effect of climate shifts and rapid urbanization in coastal and low-lying areas. Climate change is also leading to biodiversity loss, which was already pressing forward due to deforestation, industrial expansion, pollution, and population growth. Recent reports have shown unrepairable consequences on biodiversity within and between species, which threatens food security and thus further aggravate the climate change implications. For example, damage to coral reefs increases flood risk and deforestation in the Amazon increases the potential for drought and fire.

The WTO and UNEP are partners in the pursuit of sustainable development. As the principal UN agency for the protection of the environment, UNEP has years of experience in the field of climate change. The WTO has also launched its first ever trade and environment negotiation under the Doha Development Agenda. Certain climate change mitigation measures intersect with existing WTO rules and recent discussions in various for a have brought to the fore the importance of better understanding the various linkages between trade and climate change. Current status of global climate:

The scientific evidence regarding climate change is compelling. Based on a review of thousands of scientific publications, the Intergovernmental Panel on Climate Change (IPCC) has concluded that the warming of the Earth's climate system is "unequivocal", and that human activities are "very likely" the cause of this warming. It is estimated that, over the last century, the global average surface temperature has increased by about 0.74° C. Moreover, many greenhouse gases remain in the atmosphere for long periods of time, and as a result global warming will continue to affect the natural systems of the planet for several hundred years, even if emissions were reduced substantially or halted today. When greenhouse gases emitted in the past are included in the calculations, it has been shown that we are likely to be already committed to global warming of between 1.8° and 2.0° C. Most worrying, however, is that global greenhouse gas emission levels are still growing, and are projected to continue growing over the coming decades unless there are significant changes to current laws, policies and actions. The International Energy Agency has reported that global greenhouse gas emissions have roughly doubled since the beginning of the 1970s. Current estimates indicate that these emissions will increase by between 25 and 90 per cent in the period from 2000 to 2030, with the proportion of greenhouse gases emitted by developing countries becoming significantly larger in the coming decades. Over the last half century greenhouse gas emissions per person in industrialized countries have been around four times higher than emissions per person in developing countries, and for the least-developed countries the difference is even greater. The member countries of the Organization for Economic Co- operation and Development (OECD), which are the world's most industrialized countries, are responsible for an estimated 77 per cent of the total greenhouse gases which were emitted in the past.

15.2.2 Climate change impact

As greenhouse gas emissions and temperatures increase, the impacts from climate change are expected to become more widespread and to intensify. For example, even with small increases in average temperature, the type, frequency and intensity of extreme weather – such as hurricanes, typhoons, floods, droughts, and storms – are projected to increase. The distribution of these weather events, however, is expected to vary considerably among regions and countries, and impacts will depend to a large extent on the vulnerability of populations or ecosystems. A region's vulnerability to temperature changes depends on several factors such as access to infrastructure (electricity, roads and water connections) and dependence on agriculture.

Developing countries, and particularly the poorest and most marginalized populations within these countries, will generally be both the most adversely affected by the impacts of future climate change and the most vulnerable to its effects, because they are less able to adapt than developed countries and populations. In addition, climate change risks compound the other challenges which are already faced by these countries, including tackling poverty, improving health care, increasing food security and improving access to sources of energy. For instance, if we talk of India according to the World Bank, central districts in India are the most vulnerable to climate change because they lack the infrastructure and are largely agrarian. A primary reason for the fall in the incomes is climate change's effects on farmers. The monsoon and suitable temperatures are main inputs for farmers. Hot weather and disrupted rainfall hurt crop yields and, thus ruin, their incomes. According to the 2017-18 Economic Survey, extreme temperatures and droughts (defined as temperatures or rainfall loss 40% greater than the median) shrink farmer incomes to the tune of 4-14% for key crops. Poorer farmers in regions with weaker infrastructure and less irrigation are most affected.

In developing countries climate change is projected to lead to hundreds of millions of people having limited access to water supplies or facing inadequate water quality, which will, in turn, lead to greater health problems.

In 2018-19, as many as 2,400 Indians lost their lives to extreme weather events such as floods and cyclones, according to the environment ministry. The India Meteorological Department (IMD) says these events are increasing in both frequency and intensity Extreme events may be the most tangible and immediate impact of climate change, but another more long-term and equally dangerous effect is rising temperatures. In India, according to IMD data released by the statistics ministry, average temperatures have increased by 0.6 degrees Celsius (° C) between 1901-10 and 2009-18.

15.2.3 Trade-related areas particularly vulnerable to climate change

1) Agriculture

Agriculture is considered to be one of the sectors most vulnerable to climate change, and also represents a key sector for international trade. In low-latitude regions, where most developing countries are located, reductions of about 5 to 10 per cent in the yields of major cereal crops are projected even in the case of small temperature increases of around 1°C. Although it is expected that local temperature increases of between 1° C and 3° C would have beneficial impacts on agricultural outputs in mid- to high-latitude regions, warming beyond this range will most likely result in increasingly negative impacts for these regions also. According to some studies, crop yields in some African countries could fall by up to 50 per cent by 2020, with net revenues from crops falling by as much as 90 per cent by 2100. Depending on the location, agriculture will also be prone to water scarcity due to loss of glacial melt water and reduced rainfall or droughts.

2) Tourism

Tourism is another industry that may be particularly vulnerable to climate change, for example, through changes in snow cover, coastal degradation and extreme weather. Both the fisheries and forestry sectors also risk being adversely impacted by climate change. Likewise, there are expected to be major impacts on coastal ecosystems, including the disappearance of coral and the loss of marine biodiversity.

3) **Trade**

Finally, one of the clear impacts will be on trade infrastructure and routes. The IPCC has identified port facilities, as well as buildings, roads, railways, airports and bridges, as being dangerously at risk of damage from rising sea levels and the increased occurrence of instances of extreme weather, such as flooding and hurricanes. Moreover, it is projected that changes in sea ice, particularly in the Arctic, will lead to the availability of new shipping routes.

15.2.4 Climate change mitigation and adaptation

The projections of future climate change and its associated impacts amply illustrate the need for increased efforts focused on climate change mitigation and adaptation. Mitigation refers to policies and options aimed at reducing greenhouse gas emissions or at enhancing the “sinks” (such as oceans or forests) which absorb carbon or carbon dioxide from the atmosphere. Adaptation, on the other hand, refers to responses to diminish the negative impacts of climate change or to exploit its potential benefits. In other words, mitigation reduces the rate and magnitude of climate change and its associated impacts, whereas adaptation reduces the consequences of those impacts by increasing the ability of humans or ecosystems to cope with the changes. Mitigation and adaptation also differ in terms of timescales and geographical location. Despite these differences, there are important linkages between mitigation and adaptation. For instance, reforestation can serve both to mitigate climate change by acting as a carbon sink and can help to adapt to climate change by slowing land degradation. Mitigation efforts are relatively well-defined and there is considerable information available on the opportunities and costs associated with achieving a given reduction of greenhouse gas emissions. Greenhouse gas emissions arise from almost all the economic activities and day-to-day functions of society and the range of practices and technologies that are potentially available for achieving emission reductions are equally broad and diverse. Most studies addressing mitigation opportunities have, however, largely converged around a few key areas that have the potential to deliver significant reductions in emission levels. These include using energy more efficiently in transport, buildings and industry; switching to zero- or low-carbon energy technologies; reducing deforestation and improving land and farming management practices; and improving waste management. Several studies have concluded that even ambitious emission targets can be achieved through the use of existing technologies and practices in the areas identified above.

Multilateral agreement on a target for greenhouse gas stabilization in the atmosphere, as well as firm and binding commitments on the level of global greenhouse gas emission reductions that will be required to achieve this stabilization target, will be instrumental in the large-scale deployment of emission-reduction technologies and practices. Policies and measures at the national level are also essential for creating incentives for consumers and enterprises to demand and adopt climate- friendly products and technologies. Owing to awareness by government, decisions at national level eg, ban on single use plastic bags, marketers have to rework on marketing strategies in accord with the changing environment and consumers also gradually change the demand pattern for the sake of environment and health.

15.2.5 Trade as a means of economic adaptation to climate change

Climate change threatens to disrupt the conditions under which a wide range of goods and services that are important to economic well-being are produced and consumed. Trade may increase the vulnerability to climate change of some countries because it leads them to specialize in the production of products in which they have a comparative advantage, while relying on imports to meet their requirements for other goods and services. These countries may become vulnerable if climate change leads to an interruption in their supply of imported goods and services. However, trade can also provide a means to bridge the differences in demand and supply conditions, so that if climate change leads to a scarcity of certain goods and services in a country, it will nonetheless be able to obtain what it needs from countries where these goods and services continue to be available. Thus, beyond mitigation, trade can play a valuable role in helping humankind adapt to the consequences of a warmer future.

Montreal Protocol

The Montreal Protocol was established in 1987 in response to the discovery of an ozone “hole” over Antarctica, and the scientific evidence that ozone in the stratosphere was being destroyed by chlorofluorocarbons (CFCs) and other ozone-depleting chemicals. The Protocol’s primary objective is to phase-out the consumption and production of nearly 100 chemicals known as “ozone depleting substances” (ODS). Under the Protocol, both developed and developing countries have binding, time-targeted and measurable commitments, but developing countries are given longer time periods and financial assistance in meeting their targets.

Mutual supportiveness between trade and environment

The Doha negotiations on trade and environment also provide WTO members with an opportunity to consider the mutual supportiveness between the trade and environment rules, and how institutional cooperation can help foster mutual supportiveness.

15.2.6 Business to step in to confront the climate change

There is heavy pressure to mitigate and adapt to the direct impacts of climate risk and its connected risks. We witnessed climate activism in the past years, including prominence of green agendas as an electoral issue. However, multilateral progress was limited, with COP25 in Madrid ending in disappointment. Private sector is also burdened, with employees evaluating management actions on climate change and the targeting of pension funds to divest from fossil fuel assets. Investors and rating agencies have also exerted pressures on companies, whether through engagement on low-carbon transition or net zero emissions plans and investments or through inclusion of climate risks in ratings methodologies. There have also been growing demands for transparency, with financial regulators such as the Bank of England stress testing banks and insurers against climate scenarios, policymakers proposing mandatory climate risk disclosure legislation, and litigation against companies failing to disclose climate risk. Manufacturers, marketers, services providers are adopting green agendas to showcase the concern for climate.

15.2.7 Why Marketing is being discussed in the context of climate change

The whole process of marketing is designed in the framework of layers at the top lies surrounding environment, then social norms, and finally the demographic profile of existing and potential customers. The environment is constantly changing, currently humans are too much interfering with nature, deforestation in the name of development is creating havoc, and alarming pollution is falsely window dressed as industrialization. Resultantly we see adverse climate change like global warming, weather furry, rising pollution they significantly affect the demand of goods and services, and purpose behind the demand. Hence, marketing tools are to be manipulated to best serve the needs of customers either by providing innovative products or providing innovative uses of the existing products or promoting it in a manner to allure customer's attention and at the same time ensuring environment safety example electric vehicles, CNG cars.

15.3 Contemporary Issue – Food Security

15.3.1 Introduction

Food Security means that all people every time have physical & economic access to adequate amounts of food which is nutritious, safe, and culturally appropriate foods, and is produced in an environmentally sustainable and socially just manner, moreover people are easily able to make informed decisions regarding food choices. Food Security also suggest that the people who are involved in food growing, producing, processing, transporting, retailing, and serving food are earning a decent wage. At the heart of food security is access to healthy food and optimal nutrition for all. Food access is closely linked to food supply, so food security is dependent on a healthy and sustainable food system. The food system includes the production, processing, distribution, marketing, acquisition, and consumption of food.

15.3.2 Pillars of Food Security

1. **Availability:** Food availability means **supply of food** for production, distribution, and exchange. The factors which determine food production are land ownership and its use; soil management; crop selection, breeding, and management; livestock breeding and management; and harvesting. Crop production is not required for a country to achieve food security.

2. **Access:** Food access refers to the **affordability and allocation of food**, as well as the preferences of individuals and households. Poverty can limit access to food, and can also increase how vulnerable an individual or household is to food price spikes. Access depends on income, whether the household has enough finance to acquire food at given prices or has sufficient land or other resources to grow its own food.

3. **Utilization:** Once the food is obtained by a household, a variety of factors affects the quantity and quality of food that reaches members of the household. In order to achieve food security, the **food ingested must be safe** and must be enough to meet the physiological requirements of every individual. Food safety affects food utilization

and can be affected by the preparation, processing, and cooking of food in the community and household. Nutritional values of the household determine food choice, and whether the food meets cultural preferences is important to utilization in terms of psychological and social well-being.

4. **Stability:** Food stability refers to the **ability to obtain food over time**. Food insecurity can be transitory, seasonal, or chronic. In transitory food insecurity, food may be unavailable during certain periods of time such as during natural disasters, civil conflicts and droughts. Seasonal food insecurity can result from the regular pattern of growing seasons in food production. Chronic (or permanent) food insecurity is defined as the long-term, persistent lack of adequate food.

15.3.3 Food Security in the backdrop of market analyses

WFP (World Food Programme) is a renowned humanitarian organization; main purpose is to fight hunger worldwide by providing food assistance in emergencies and by working with communities to improve nutrition. It is committed to end hunger and provide food security and nutrition by 2030. In countries where WFP complements national efforts in combating food insecurity, the organisation's interventions are significant in the domestic food sectors. Being a player in the food sector, it is important for WFP to have a sound grasp of the basics of the food sector, including keeping abreast of the food security situation and relevant market intelligence.

The understanding of market analysis in a food security context is intended to achieve the following objectives;

- To highlight the significance of market analysis for the planning, implementation and evaluation of food security interventions and their impact
- To impart basic knowledge on the key aspects of market analysis in a food security context; and
- To prepare and enable WFP and counterpart staff to conduct basic market analysis in a food security

MARKET

From a general point of view, a market refers to the set of all sale and purchase transactions that affect the price of a commodity. In other words it is an interaction between demand and supply of a good or service and it entails consumers, suppliers, transactions and the factors that affect them

ANALYSING MARKETS

In general, markets are analysed for the purpose of understanding;

1) The system within which they operate (centrally planned, free, mixed)

2) How they are structured (market players are predominantly large-scale traders, small-scale individual traders, large companies or farmers' associations/cooperatives etc)

3) The extent to which their actors are concentrated (perfect competition, pure monopoly, oligopoly, monopolistic competition).

4) The extent to which they are accessible to both sellers and buyers. Market accessibility and connectivity is defined in terms of the infrastructure that links the market to other markets, the markets to production areas and markets to consumers, the status of connectivity and accessibility largely influences the prices of goods, in extreme cases the market could cease to exist if connectivity is poor or non-existent. In remote areas where this is often the case, poor market accessibility often leads to an increase in food insecurity either through a total lack of supplementary sources of food to complement people's own production or through high food costs that household's are un-able to afford. Poor market connectivity also hinders households' ability to earn in-come from cash crop sales thereby impacting on their food security. In many instances market accessibility and connectivity vary significantly from season to sea-son (e.g. due to events such as impassable roads during the rainy season, etc), thereby triggering seasonal variations in the supply of produce and resultant market price variations.

5) Whether they are connected and integrated with each other

An integrated market is one whose composite market locations are inter-connected (in terms of physical and communication infrastructure) with fewer barriers to en-able efficient flow of goods and services. The interconnectivity among composite market locations lessens transaction costs and enhances efficient price transmissions among various market locations. As a result, an integrated market is characterised by harmonised price patterns of a particular commodity in the various com-posited market locations. For the purpose of these notes the term ***market integration*** will be used to refer to what is generally known to be ***spatial market integration***. A spatially integrated market is characterised by commodity price trends at different market locations that follow a similar pattern over an extended period of time (i.e. at least 2 agricultural seasons). Some of the advantages of an integrated market include: enhanced security of supply, reduced price risks, reduced market entry barriers leading to increased numbers of suppliers etc

6) The policies and rules that regulate their functioning

When building a market profile it is always important to take into consideration prevailing government policies and regulations that either directly or indirectly impinge on the market's processes. Such policies and regulations could either facilitate or hinder a market's performance and functioning. In general, governments intervene in a market for a number of reasons. These may include; fiscal purposes (e.g. imposition of taxes/duties), political purposes (e.g. consumer subsidies to contain probable riots), development purposes (e.g. producer subsidies or import duties to protect nascent domestic industries).Before conducting a market analysis, it is imperative to first understand how the market is organised and how it functions. The characteristics of a market system will have a significant effect on how the market itself operates and responds to both endogenous and exogenous effects. The first step of market analysis therefore is to gather information on its basic characteristics in order to build a market profile to understand how it is structured and how it operates and influences the food security status of those who depend on the market.

Building a Market Profile

In building a market profile, one has to gather information on the following key components namely; the market system, market structure, market concentration, market accessibility and connectivity, market integration and government policies and regulations that impact on the operation of the market. The following sub-sections provide an explanation of the key constituents of a market profile (in a food security context.

15.3.4 Relevance of marketing in ensuring Food Security

The three major components on the supply side of a nation's food balance sheet (that best estimates a country's food security status) are:

- Domestic food stocks and production capacity;
- Capacity to import adequate food to meet food gaps; and if not adequately covered
- Food aid as an alternative to help bridge the gap

For the first two components that constitute the core of a nation's food security, the market is pivotal in ensuring that the two components fulfil their respective roles through the efficient movement of food from where it is produced or imported to where it is consumed.

As economies grow, the proportion of households that are net consumers of food tends to outgrow the number of those that are net producers of food (i.e. with their own food production exceeding household food consumption requirements). In many developing countries, disasters further increase the number of net-consuming households by reducing household food production. From both points of view, the implication is that more and more households worldwide are increasingly relying on markets to meet their food demands. The role of markets has become vital in any nation's food security. Therefore, the understanding of how markets function has become equally important for those stakeholders involved in dealing with national and global food security.

In the developing world, the food aid component of a country's food balance sheet may constitute a complimentary but vital part of the national food security. In such instances, careful advance planning becomes paramount since food aid can have serious repercussions on a nation's food production and food markets if not appropriately implemented. WFP is the largest food assistance organisation in the world and its policy commits the organization to the use of food aid in situations where it has a comparative advantage and where food aid does not negatively impact local food production and food marketing systems.

In the context of a strategy of a nation's food security, market analysis should serve the purpose of providing tools for:

- Estimating national/regional/local food supply capacities/potentials against domestic requirements;
- Determining market response capacities to cover national food demand gaps; early warning in cases where domestic food production and food markets are unable to adequately cover national food demand gaps; and
- Designing policy recommendations to national governments and informing the corporate policies of global food aid actors on global and national food security strategies.
- In the specific instances of food aid provision at a national level, market analysis in a food security context may provide tools for:
- Planning food aid interventions with the assurance that their impact on local food production and food markets is not a negative one;
- Making the appropriate decision on whether cash/vouchers or food aid is the best suited option to address prevailing food insecurity; and
- Planning local or regional food purchases and ensuring that these are implemented at the optimal time with maximum developmental effect on domestic producers and markets

Applied market analysis in a food security context should always deliver results that are clear, understandable and relevant to efforts being made in addressing food insecurity. Therefore, the results of a market analysis for food security should provide clear answers and evidence-based recommendations on the following questions:

- From the market perspective, what long-term solutions exist to address food insecurity? What is the capacity of local markets to meet prevailing food demand?
- Is food aid the best option of intervention to address food insecurity among the targeted population; if not, what are the alternatives?
- If food aid is the appropriate response, then what quantity would not distort markets and cause producer disincentives, with what commodities (local tastes), and when would it be best to intervene?
- Is the local/regional procurement of food aid feasible?
- If the local/regional procurement of food aid is feasible; when should it be conducted, what commodities should be procured, how much should be procured, from which markets, from whom, and at what prices, what procurement arrangements would maximise the impact on farm household incomes and on developing local food markets?

15.4 Contemporary Issue – Geopolitics

15.4.1 Introduction of Geopolitics

Geopolitics is the analysis of the geographic influences on power relationships in international relations. The word *geopolitics* was originally coined by the Swedish political scientist Rudolf Kjellén about the turn of the 20th century, and its use spread throughout Europe in the period between World Wars I and II (1918–39) and came into worldwide use during the latter. In contemporary discourse, *geopolitics* has been widely employed as a loose synonym for international politics. At the international level relations, geopolitics is a method of studying foreign policy to understand and predict international political behaviour through different geographical variables.

These include area studies, climate, topography, demography, natural resources, and applied science of the region which is being evaluated. Geopolitics focuses on political power related to geographic area. In particular, territorial waters and land territory in correlation with diplomatic history. Geo-politicians sought to understand how the new industrial capabilities of transportation, communication, and destruction—most notably railroads, steamships, airplanes, telegraphy, and explosives—interacting with the largest-scale geographic features of the Earth would shape the character, number, and location of viable security units in the emerging global international system.

Geopolitical elements constitute an important component of the external environment affecting international business operations. Together with other environmental variables, they are likely to influence a firm's decisions on its future or existing international business activities. However, there are few studies highlighting the geopolitical milieu that affects the international business domain. A framework for a geopolitical paradigm of international business is introduced with a particular focus on the time, place and demographical dimensions of geopolitics.

15.4.2 Geopolitical variables and international business

Time dimension

The international distribution of power among states shifts continually as one historical period gives way to another. The international geopolitical environment has been changing constantly affecting international business dynamics. Any specific change in this environment at a particular point of time may influence the operations of international business within, as well as beyond, that time frame. It is important, therefore, for the international business firm to monitor these changes and to respond to them accordingly and in a timely manner.

Place dimension

From the geopolitical perspective, relationships among states are influenced by an area's strategic value. This value, however, depends on the importance of an area in terms of its natural resources, size, and proximity and future prospects in relation to other countries.

For example, Australia's relationship with New Zealand bears more strategic value than its relationship with Sri Lanka. Because of the geographic proximity of Australia to New Zealand, their relationship in terms of each other's political, economic and security interests is more critical than Australia's relationship with many other countries. In addition, the size of countries matters. Indonesia, one of the most populous countries in the world, and largest among Australia's neighbours is very important to Australia. In addition to its large population base, Indonesia is endowed with natural resources. However, geographically, Australia belongs to the larger Asia-Pacific region. Geographic consideration in terms of proximity, convenience and strategic directions such as long-term prospects and transactions cost factors are vital in explaining this regional setting. Every political community has a geographical base. Each political community is set on a territory that is a unique combination of location, size, shape, climate and natural resources. Thus, most transactions among nations entail significant, even crucial, geographical considerations. Four major aspects of the place dimension - natural resources, strategic location, geographic proximity and regionalism.

Natural resources

Availability of natural resources is a significant geopolitical variable. The primary thrust of colonial excursions was to search for and exploit these resources Foreign companies find it convenient to invest in countries with these advantages because it significantly reduces their transactions costs of importing raw materials through the vertical integration (market internalisation) process. Resource-seeking multinationals tend to be highly vertically integrated firms.

Strategic location: Location is likely to be a critical international business consideration. British political geographer Sir Halford MacKinder, in his famous

“Heartland’ theory proposed that north-central Eurasia, because of its geographically strategic location and vast natural resources, would eventually be the heart of the world’s controlling political and economic power. This theory crystallised the importance of strategic location. Singapore, exemplifies this case. As a tiny citystate, Singapore has positioned itself as one of world’s most dynamic economies. Singapore’s strategic location is said to be primarily responsible for its success. Given Singapore’s strategic positioning, it is known as an ‘entrepôt’ centre in that much of the country’s trade comprises the transhipments of goods produced in the region. Because of its strategic location, it also hosts most of the regional headquarters of the foreign multinationals. Considering its apparent geographic importance, in 1989, Singapore became a part of the Southern Growth Triangle (SGT).

Geographic proximity

Physical distance is generally considered to be one of the major factors that constitutes the core of the geopolitical dimension. It is likely that geographic proximity enables companies from neighbouring countries to engage in international business activities more frequently than their physically distant counterparts. Countries within a close proximity are considered to be psychologically ‘near’ to each other, facilitating trade and investment among themselves. That is, foreign companies often seek out business in countries that are within a close physical proximity. For example, the largest and fourth largest trading partners of the US, viz. Canada and Mexico, are located on its borders. Many American plants are located on the Mexican side of the common border. These business arrangements incur relatively lower transactions costs, in that they confront fewer major changes of socio-cultural environments.

Regionalism

Despite the reality that communication has overcome many of the restrictions formerly dictated by distance, regionalism has gained momentum during recent years. Now, the boundaries of regional entities are more extensive than before, primarily a result of improved communication and transportation systems. Intra-regional trade and investments are becoming increasingly popular due to preferential trade advantages. For example, more than 95% of the world's recorded foreign direct investment (FDI) flows from countries that are members of the Organisation for Economic Cooperation and Development (OECD), and about three-quarters of this total is invested in other OECD countries. Because of special privileges for investors from within a regional forum, intra-regional FDI is also prevalent in the other regional forums, such as the Asia Pacific Economic Cooperation (APEC), European Union (EU) and the North American Free Trade Agreement (NAFTA). Formalised regionalism does encourage foreign investment within the region, and firms are lesser inclined to invest in a country in a different and distant region, *ceteris paribus*.

Demographic dimension Population as an important geopolitical variable. He considered its various characteristics, particularly the qualitative and ideological, as the major demographic factors that influence the geopolitical milieu. The population characteristics of a country are important because the skills, educational qualifications, productivity and the cost of labour play a role in determining how a country fits within the global business environment. The ethnic and religious features of a population may affect the bilateral or international relationships of a country. The Tamil movement in Sri Lanka or the Jammu and Kashmir disputes in India may be explained from this perspective. Also, the size of a population matters. These demographic factors have been contributing substantially to the motivation for opting for a particular mode of international business operation. Discussions on these issues given below:

- **Size of the population:** The size of a population may be considered an important motivator for international business growth. With a population of around 18 million persons, Australian businesses have limited scope to grow domestically and this motivates many Australian firms to invest overseas. It may affect inward investment as well. The small population base of New Zealand (about 3.5 million) has been shown to be the primary reason for the limited long-term business growth and decreasing Japanese investment in New Zealand . On the other hand, the huge population base in India is a motivator for foreign investors to invest there on a long-term basis.

- **Supply of labour:** The supply of labour is another demographic variable closely related to the population size. It is perceivable that a larger population will produce a larger supply of labour, which in turn, will create a competitive labour market and low labour costs. It has long been observed (e.g. that countries with low labour costs are attractive locations for foreign investors. However, labour productivity is critical. In 1871, Ricardo identified labour productivity and wage rates as two determinants of a country's comparative advantage. Technologically developed countries have a pool of labour more productive than those of the developing countries, whereas, the labour force in developed countries tends to be more expensive than that of the developing countries. The human development index (HDI) developed by the United Nations provides an insight into the quality of life across the nations of the world. Based on indicators such as literacy rates, the number of inhabitants per doctor, infant mortality rates, life expectancy, calorie (food) consumption per capita, car ownership per 1000 people, and education spending as a percentage of GDP, HDI also reflects the quality of labour in a particular country.

For example, it may be argued that the availability of cheaper labour in India would make this country an attractive investment destination for Australian companies. Also, India has a large pool of technologically skilled people. However, low productivity of the Indian labour forces has been a concern for foreign investors.

Role of Environmental, Ethnic and Religious Groups

These are additional demographic factors that are likely to affect the international business environment. There are many environmental groups around the world attempting to safeguard their natural environments. Pollution control, through to the maintenance of natural habitats for endangered species are within the agendas of these organisations. These organisations campaign on various country-specific, regional and international fronts. The World Wildlife Fund (WWF), Greenpeace and many other country-specific and regional organisations are involved with such movements and these activities can impact international business decisions. Ethnic and religious alignments are the two other major demographic factors. The conflicts between Serbs, Croats and Muslims in Bosnia-Herzegovina epitomises the effects of ethnic and religious conflicts on a national economy as well as the risks associated with doing international business in these economies.

15.4.3 India's Biggest Geopolitical Challenges

- **China:**

Pakistan is no longer the biggest challenge, but China. India could still lock horns with China in other regions. In 2013, Vietnam offered India seven oil blocks located in the South China Sea. The South China Sea is rapidly becoming the most dangerous area on the planet, with acts of aggression between nations reaching an all-time high. Already, China, Japan, Vietnam and the Philippines are engaging in hostile acts to maintain their regional security. This situation then, has the potential to pull India in, either in defense of its oil blocks, or in defense of a neighboring nation asking for support. In either case, India will be entering the South China Sea militarily, and this will push New Delhi to directly challenge the dominance, influence and power of Beijing.

As Noval Covid-19 epidemic is spreading across the world, the virus is supposedly originated from Wuhan Research Labs. If the news has even iota of veracity it would give birth to geopolitical tension and would adversely affect the trade. Already India China trade declined by 12.4% in the first two months of corona virus outbreak i.e. from January 2020 to February 2020. (Economic times)

- **Pakistan:** While Pakistan has always been a geopolitical challenge for India, Pakistan itself faces an unprecedented internal turbulence and chaos. Pakistan is being torn apart by radical groups, disease, a stalling economy and a declining list of allies. Besides China, Pakistan's regional friends are limited and in the coming years, Pakistan will need regional partners more than ever.

Kartarpur corridor– a Positive step : The Kartarpur corridor is a 2.5 mile stretch that links Indian pilgrims with Gurdwara Darbar Sahib in Kartarpur in the Narowal district of Pakistan, which is considered the second holiest site in Sikhism as it is believed to be the place where Guru Nanak, the founder of Sikhism, spent the last 18 years of his life. The ***gurdwara***—which means a "gateway to the guru"—thus holds tremendous religious and sentimental value to the Sikh community. The corridor is expected to bring India Pakistan closer and improving the political and economic relations. As it was a transforming decision which on one hand would attract big investment in Pakistan and on the other hand would satisfy the religious sentiments of Indian Sikh and non Sikh community.

Charging of fees, beurocratic hurdles, fear of illegal movements over the path are still hampering the real objectives of the. Also, Frequent ceasefire violations are adding to troubles , hence it is dicey whether the corridor would do things better or not.

India asserts its interests regionally and globally. Flourishing of India as powerful country will increase dependence of Pakistan on India for trade, investment and other means. Owing to international political strength, our country has laid indelible mark at global level as a result we are being favoured by other developed countries against Pakistan. This might push Pakistan-India ties to a new level, one could see India and Pakistan moving away from the chaotic relationship they once shared to a relationship that is dynamic, positive and secure.

- **Holmuz State Dispute:**

The impact of ongoing geopolitical tensions in the Strait of Hormuz is already being felt in the cruise industry and could spill over to wider trade if oil prices are affected. The State of Hormuz, bounded by Iran, Oman and the United Arab Emirates (UAE), connects the Gulf with the Arabian Sea. The waterway is a key shipping route for oil tankers as approximately one fifth of the world's oil traffic, nearly 21 million barrels a day, passes through the strait. The channel is equally important to the logistics industry with large numbers of container ships transporting cars, white goods and food to Jebel Ali in Dubai, the busiest port in the Middle East. A narrow stretch of water less than 100 miles long and 21 miles wide at its narrowest point is currently the focus of intense efforts led by the United States aimed at protecting trade and security in the Gulf region.

The Strait of Hormuz, bounded by Iran, Oman and the United Arab Emirates (UAE), connects the Gulf with the Arabian Sea. The waterway is a key shipping route for oil tankers as approximately one fifth of the world's oil traffic, nearly 21 million barrels a day, passes through the strait. The channel is equally important to the logistics industry with large numbers of container ships transporting cars, white goods and food to Jebel Ali in Dubai, the busiest port in the Middle East. In recent months, America and Iran have been engaged in brinkmanship in the aftermath of the US withdrawal from the Iran nuclear deal in May 2018. Iran's Islamic Revolutionary Guards seized an Iraqi oil tanker in the Gulf on suspicion of smuggling fuel. The tanker was reportedly carrying around 700,000 litres of fuel. Iran claims monopoly over its security, which means there are significant structural problems the Strait of Hormuz faces.

15.5 Contemporary Issue: Sustainable Development

15.5.1 Sustainable Development

"Sustainable development is development that meets the needs of the present

without compromising the ability of future generations to meet their own needs."

But the focus of sustainable development is far broader than just the environment. It's also about ensuring a strong, healthy and just society. This means meeting the diverse needs of all people in existing and future communities, promoting personal wellbeing, social cohesion and inclusion, and creating equal opportunity. Sustainable development is about **finding better ways of doing things**, both for the future and the present. We might need to change the way we work and live now, but this doesn't mean our quality of life will be reduced right now.

A sustainable development approach can bring many benefits in the short to medium term, for example: Health & Transport - Instead of driving, switching to walking or cycling for short journeys will save you money, improve your health and is often just as quick and convenient.

15.5.2 How business support the pillars of sustainable development

Business organisation does not exist in the vacuity; it takes both natural resources from the environment and human resources from the society, and in turn provides the converted produce to the society, for betterment of humans and thus give life to the economy. When we synthesise the business activities we will find that it has inherent capacity to participate in sustainable development. We might get clear picture from the pillars of sustainable development discussed below-

The term sustainability is broadly used to indicate programs, initiatives and actions aimed at the preservation of a particular resource. However, it actually refers to four distinct areas: human, social, economic and environmental - known as the four pillars of sustainability-

1-Human sustainability:

Human sustainability aims to maintain and improve the human capital in society. Investments in the health and education systems, access to services, nutrition, knowledge and skills are all programs under the umbrella of human sustainability. Natural resources and spaces available are limited and there is a need to balance continual growth with improvements to health and achieving economic wellbeing for everyone.

2-Social sustainability:

Social sustainability aims to preserve social capital by investing and creating services that constitute the framework of our society. The concept accommodates a larger view of the world in relation to communities, cultures and globalisation. Social sustainability focuses on maintaining and improving social quality with concepts such as cohesion, reciprocity and honesty and the importance of relationships amongst people. It can be encouraged and supported by laws, information and shared ideas of equality and rights.

3-Economic sustainability:

-

Economic sustainability aims to maintain the capital intact. Economic sustainability aims to improve the standard of living.

"Maintaining high and stable levels of economic growth is one of the key objectives of sustainable development. Abandoning economic growth is not an option. But sustainable development is more than just economic growth. The quality of growth matters as well as the quantity."

4-Environmental sustainability

Environmental sustainability aims to improve human welfare through the protection of natural capital (e.g. land, air, water, minerals etc.). Initiatives and programs are defined environmentally sustainable when they ensure that the needs of the population are met without the risk of compromising the needs of future generations.

15.5.3 India and sustainable development goals

The Sustainable Development Goals (SDGs) were adopted in September 2015 as a part of the resolution, 'Transforming our world: the 2030 Agenda for Sustainable Development'. India is committed to achieve the 17 SDGs and the 159 associated targets, which comprehensively cover social, economic and environmental dimensions of development and focus on ending poverty in all its forms and dimensions. At the Central Government level, NITI Aayog has been assigned the role of overseeing the implementation of SDGs in the country.

To spread awareness about the Goals, bring together stakeholders and build capacities for the realization of SDGs, NITI Aayog has organized several national and regional level consultations.

15.5.4 Government initiatives for environmental protection

1.Ban on Plastic Bags: Forest and Environmental Ministry of India has ordered to retail outlets like Bigbazaar, MORE, CENTRAL, D.MART, etc that they provide jute bags , paper carry bags, only if customer is ready to pay for it and cannot provide any plastic bag to customers.

2. Green IT Project by SBI: By using eco and power friendly equipments in its 10000 new ATMs, the Banking giant has not only saved power costs and earned carbon credits, but also set the example for others to follow. SBI entered into green service known as "GREEN CHANNEL COUNTER". SBI provides many services like paperless banking, no deposit slips, no cheques, no money transaction forms. All these transactions are done through SBI Shopping and ATM cards.

(i)Eco friendly rickshaws before CWG: In order to promote eco friendly transportation in the city ahead of Common Wealth Games eco friendly rickshaws were launched by Chief Minister of Delhi Sheila Dixit. These rickshaws are called E-RICKS & these are battery operated.

4. Various standards for environment protection: The Government has set up various standards for environment protection such as energy efficiency standards for appliances (refrigerators, air conditioners, tube lights, transformers, and other electrical appliances), energy conservation building code (ECBC), and fuel efficiency/emission norms for vehicles.

5. Government increasing forest area: Government, both at the state and centre, is making efforts to achieve the target of India's 33% land under forest cover. At present, 24% of India's land is under forest and tree cover.

6. Certifications and awards: Government is Imposing strict Rules and Regulations for pollution control. Consideration of Pollution control efforts and eco technology in awarding IS, ISO 9000, or ISO 14000 certificates and other awards.

15.5.5 Some latest trends related to sustainability in India

1. The push for a cleaner environment: When the Swach Bharat Abhiyaan was launched 6 years back, many viewed it with skepticism. Whether it can be deemed a success or not, no one really knows at the moment, but one thing is for sure, it has brought the discourse on cleanliness to the mainstream. 39% of companies we studied have allocated funds to this campaign and built toilets or helped in cleaning up of public spaces. Major newspapers now allocate space to the need to build public toilets, garbage burning, littered roads and even large public events that cause environmental damage and filth. In part, this has also been led by larger public awareness due to health hazards of water and air pollution.

2. CSR as strategy and not charity: Corporate India is finally realising that the short term approach of writing a cheque for the CEO’s favourite charity is not prudent any more. Since CSR investments need appropriate disclosure and need to be done every year 2016 saw many companies holding back CSR funds if they didn’t find appropriate projects. Less than 4% of CSR funds spent by top Indian corporates was given as charity as per our study. Companies are now looking at methods to add strategic brand value through these investments even if these are not directly related to the business they are in, as required by law.

3. ZERO IMPACT moves to NET POSITIVE: Most companies are moving towards creating sustainable growth models in different ways. As manufacturing companies explore the inter linkages of supply chains it is evident that waste, water, energy and materials are closely linked to business continuity. There is a growing realization that growth without adversely impacting the environment is now an expected goal. Forward looking companies like Ambuja Cement, ITC, Dalmia Bharat , etc., are talking of being water positive several times over.

4. Water begins to take centre stage: Droughts and water shortages in one area and extreme floods in other parts were part of the ongoing discourse around Indian cities and villages in 2016. Companies have had to increasingly gear up to the challenges this has posed. From stopping operations and facing large scale damage in flooded areas to sourcing water trucks for employees and regular manufacturing operations, water is now becoming a significant risk factor. Water is now one of the highest global risks, according to the ninth edition of the Global Risk Report, released in early 2014 by the World Economic Forum. Corporate sustainability reports, are now speaking of water at two levels – as part of CSR initiatives for communities and as part of company operations.

5. Renewable gather momentum: With the Paris accord in play, companies will need to pitch in, in a significant manner for India to achieve the NDC (Nationally Determined Commitment) of emission cuts by 33-35%. Hence it is expected that companies would focus more and more on renewable with a strong focus on solar, bio-fuels and wind. Off the grid energy systems are likely to provide succour to remote areas, which remain deprived of electricity supply. This is likely to gain strength with developments in energy storage. Improved storage will also help corporations move towards renewable energy for their own consumption. Corporations will increasingly engage with the government in policy making and contribute towards an effective public-private partnership on renewable.

6. **Only the top 33% companies believe in taking the long term view on responsible business**

For the longest time Indian companies have focused on market access, customer acquisition and compliance. There is now however a shift towards a more responsible form of growth because taking a long term view of sustainability and social responsibility is creating long term competitive advantages and helping in managing risks. Top companies have a deeper focus on Governance, Disclosure, Sustainability and CSR. However, the lower ranked companies have not seen a significant change.

7. Companies look at long term projects and not charity: 32% companies spent 2% and more in 2014-15 on CSR activities, higher than 18% in the previous year of study. Further 33% companies spent between 1% and 2% of their average PAT. And remaining 35% companies had a CSR spend of less than 1% of their average PAT. Aggregate CSR spend for 173 companies in 2014-15 was Rs. 5752 cr with an average spend of Rs. 33.25 cr per company. This translated into an average CSR spend as a percentage of average PAT of 1.4%, which is lower than the Government mandate of 2% and more.

8. Government push makes corporate India step up

The Companies Act of 2013 and several government initiatives have pushed companies to work in relevant areas. Improved compliance on account of spending requirements, CSR committee requirements, reporting requirements etc

Swachh Bharat Swasth Bharat – The mission has been taken up by companies across the country with some success. About 39% of the companies surveyed have a focus on Swachh Bharat – primarily focused on construction of toilets.

Solar – The push toward renewable has been another focus area for the government. We find that 59% of the companies surveyed work in the areas of solar energy.

15.5.6 Successful Indian companies adopted sustainable development

1. Patanjali Ayurveda Ltd.: an Indian FMCG company. Its headquarter and manufacturing unit are located in the industrial area of Delhi and Haridwar respectively. The company manufactures mineral and herbal products. The company imports majority of herbs in India from the Himalayas of Nepal. According to CLSA and HSBC, Patanjali is the fastest growing FMCG Company of India.

2. Use of Wind Energy by SBI: SBI turns to wind energy to reduce emissions. The WIND project is the first step in State Bank of India's Green Banking Programme dedicated to the reduction of its Carbon Footprints and promotion of energy efficient processes, especially among bank clients. In phase-I windmill operation 9MW in

Maharashtra, 4.5 MW in Tamil Nadu, and 1.5MW in Gujarat. Additionally 20 MW windmills to be installed in Gujarat shortly.

3. Lead free paints from KANSAI NEROLAC: Kansai Nerolac has worked on removing Hazardous heavy metals from their paints. These metals are lead, mercury, chromium, arsenic and antimonym which can have adverse effect on humans. These can cause damage to Central Nervous System, Kidney, and Reproductive system

4. WIPRO's Green Machines: WIPRO Info. Tech. was India's first company to launch environment friendly computer peripherals. For the Indian market, Wipro has launched a new range of desktops and laptops called WIPRO GREEN WARE.

5. Going Green TATA's New Mantra: TATA Motors is setting up eco friendly showrooms using natural building material for its flooring and energy efficient lights. However this project is at its preliminary stage.

6. HCL: HCL is another brand that is trying to introduce eco- friendly products in the market and it has recently launched the HCL ME 40 notebooks. These notebooks do not use any polyvinyl chloride (PVC) material or other harmful chemicals and the Bureau of Energy Efficiency already given it a five star rating.

7. Haier: Eco branding is a part of Haier's new green initiative and they have launched the Eco Life Series. They have semi automatic and automatic refrigerators and washing machines, split and window air conditioners and a lot more.

8. Samsung: Samsung India has always had a roaring range of LED TV screens and now they have come up with eco- friendly LED backlight. They use 40% less electricity having no harmful chemicals like mercury and lead.

15.5.7 How business can support the economic pillar of sustainable development?

Over the past few decades, we've seen the significant role of global trade in reducing poverty, creating jobs, and promoting growth. The number of people living in extreme poverty was cut in half between 1990 and 2015. Trade helps provide more and better jobs to people, lower prices for products, and stimulate the growth necessary to end poverty.

- **Effect of trade on social interests?**

The effect of trade on social interests is more mixed. The economic benefits of trade can empower people to address major social needs in their communities, like protecting human rights, improving working conditions, and achieving gender equality. Further, trade agreements and rules also have the potential to serve as social safeguards.

- **How trade can help the Environment?**

The relationship between trade and the environment is complex and certainly not always positive. For example, the global agricultural trade has caused agricultural expansion, deforestation, and biodiversity loss in producer countries. Exports of soya and palm oil bring revenue to countries like Brazil, Indonesia, and Malaysia, but the intensive farming of these crops also causes rainforest and habitat destruction, over farming, and the destruction of soil and water.

- **Trade may also be an obstacle to combating climate changes:**

Open trade would increase industrial production and eventually increase CO2 emission Also, "trade may increase the vulnerability to climate change of some countries because it leads them to specialize in the production of products in which they have a comparative advantage, while relying on imports to meet their requirements for other goods and services. These countries may become vulnerable if climate change leads to an interruption in their supply of imported goods and services."

15.6 Contemporary Issue – De-Globalization

15.6.1 Introduction

De-globalization has been regarded as a process of diminishing economic interdependence and integration between countries. Consequently, the term is used to describe several past periods, when the flows of foreign direct investment (FDI) and the capacity of international trade were declining due regional or global economic crises.

Discouraged by the incapacity of globalization to find solutions to some vital issues of the global economy (such as poverty, unemployment, decline and restructuring of entire economic sectors etc.), a series of researchers and practitioners felt compelled to witness the profound degradation of several historically constituted economic and social structures, which, until then, seemed to be unwavering. Accordingly, they swiftly proceeded to the definition and implementation of a new term which, for lack of other notions, was termed "de-globalization". This situation represents to a certain extent an option for survival and not necessarily a plea for revisiting the age of economic protectionism.

15.6.2 Measuring De-Globalization

Indeed, one of the constant issues of economic theory and practice refers to the method of measuring the de-globalization phenomenon. Similar to globalization, a set of indices can be taken into account in order to reveal the facets of the phenomenon of de-globalization. Contemporary economic research postulates that the process of de-globalization can be best highlighted by watching at least three main economic flows, such as:

- Dynamics of imports and exports of goods and services at a global or regional level, as an expression of international commerce.
- Dynamics of expats' money remittance.
- Inflows and outflows brought by foreign direct and portfolio investments.

Monitoring -these three macroeconomic components alone does not give a clear enough picture of the de-globalization process. The analysis must also rely on additional information, such as of changes in technology transfer, evolution of tariffs and non-tariff barriers to trade, restrictions imposed by some states on the free movement of labour, elaboration of administrative acts meant to encourage the purchase and consumption of local goods, subsidies offered to protect the agricultural sector etc

15.6.3 Causes of De-Globalisation

In recent years, our economic system is being increasingly globalized fostering a permanent flow of goods and people across borders. This is manifested in the creation and expansion of free-trade zones such as the European Economic Area (EEA), the North American Free Trade Agreement (NAFTA), and the ASEAN-China Free Trade Area (ACFTA), which reveal the architecture of a unified global market.

Global exchange of goods, services, capital, idea and information successfully increasing overall consumption, enhancing productivity, leading to cost efficiency and participating countries are gaining from globalisation then why are we confronting signs of de-globalisation? Britain's divorce from European Union, new turn toward protectionism as a haphazard consequence of the narrow outcome of the 2016 US presidential election and the victory of Donald Trump, collapsing of Soviet Union, these examples of undergoing disintegration shows that the countries want to flourish independently. The causes of De-Globalisation are-

- **Political Issues**: As a reaction to the globalized economy, some political movements have confrontationally emerged in recent years. Major episodes such as the Brexit referendum or the elections of Donald Trump in the United States and Bolsonaro in Brazil , as well as the outcome of other minor elections and referendums across Europe and the Americas, show that these trends are relevant. These episodes are the start point of a deglobalization process all around the world, which is evidenced by misalignment and confrontation between people and the Establishment. Also Natural events such as forest wildfires or the consequences of earthquakes in some regions eventually manifest catastrophic dimensions and huge regional differences that go beyond the phenomenon itself.
- **Economic Issues**: The collapse of centralized systems has been evident in political governance as it happened in the former republics of the Soviet Union.

These countries were centrally planned economies, which were managed by a reduced number of people. However, their over-centralized power tended to amplify the corruption effects from the central state agencies. Additionally, the overload of bureaucracy and the excessive concentration of administration tasks and responsibilities slowed down economic abilities to respond and adapt to the requirements of both the market and people. It constrained economic development and led to a systemic inefficiency of the whole government.

It was observed in the recent economic crisis in Europe, where the financial systems of all the member states were highly interconnected. Thus, despite the efforts and mechanisms of the European Union (EU) authorities for avoiding a contagion effect, the opening of new and critical paths for risk transmission was evident. EU authorities had to approve multiple and substantial financial bailouts to Greece since early world financial crisis ($146 billion in 2010, $172 billion in 2012, $86 billion in 2015) despite the Greek economy accounts for less than 2% of the EU GDP (with around $200 billion in 2017) . Even so, the collapse risks could not be fully controlled. So, debt crises also resulted in de-globalisation. In the present, consequences of such collapse have clearly reached beyond the initial economic crisis into the socio political sphere. Strong reactionary movements, mostly nationalists, have accompanied the austerity policies implemented across the region. Within complex systems theory, these de-globalization movements are signalling the need for a reduction of interdependencies among national economies.

- **National Interest**

Several countries want to go back to economic and trade policies that put their national interests first. These policies often take the form of tariffs or quantitative barriers that impede free movement of people, products and services among countries. The idea behind all this protectionism is to shield local manufacturing by making imports costlier. The present talk around ‘trade war’ and ‘de-globalisation’ cropped up after the US, in March, imposed 25 per cent and 10 per cent duty on steel and aluminium imports, respectively, from certain countries, citing national security and job creation as the triggering factors.

A 25 per cent tariff was then imposed on over 1,300 other Chinese products. China hit back by imposing additional levies on a range of American imports, including walnuts, raisins and almonds. The value at stake in the US-China trade wars range from $100-150 billion. The European Union too has jumped into the fray, with a 25 per cent duty on certain US products.

- **Security Concern**: Increased exchange and mutual trade between nations have made it increasingly tough to maintain global security. Terrorist organisations like ISIS and Al-Qaeda that are anti-globalisation at their core, use tools of globalisation such as the internet to propagate their agenda. Each terrorist attack that takes place in these developed nations brings more people in support of de-globalisation. The public in the developed nations feels that the consequences of free trade and cooperation with nations are too high. To cut off from rest of the world feels safer. Self-Protectionism seems to be rising. Tackling rising security concerns was a prominent part of Donald Trump's plan to "Make America Great Again". His executive order to put a travel ban on six Muslim majority nations, even though criticised and finally revoked, was a step towards Self-Protection and a sign of de-globalisation.

- **Refugee Crises:** The Syrian civil war and constant unrest in western Asian nations have caused a severe refugee crisis. The majority of the citizens from these nations have taken refuge, legally or illegally in European nations. The government of most European countries are burdened with the additional responsibility of providing for these refugees. This is a huge cause of concern for these debt-stricken economies. When these economies are unable to grow or create enough employment opportunities for their own people then the voice against globalisation grows stronger. The United Kingdom's exit from the European Union is a similar story of self-protectionism and a step towards de-globalisation.

15.6.4 Globalisation- Blessing Indeed

Globalisation created millions of jobs for Americans and provided the perfect platform for expansion of their companies by taking advantage of cheap labour in developing nations, like India. Majority of the nations still support and believe in globalisation today and they believe it would hurt our country economically, socially and politically. Adverse impact of de-globalisation is as follows

1) **Economic impact:** De-globalisation will lead to reduction in the rate of economic growth of India.

- It will lead to protectionism with reduced collaboration among countries that will hurt Indian trade and exports.
- De-globalisation will lead to reduction in competition and raise in general prices of the goods and services.
- It will destroy employment opportunities because as it will prevent outflow of skilled people due to protectionist measures like visa regulations. This will impact their employability and remittance to the nation.
- It may lead to increased import costs due to lesser choice and options and manufacturers and producers would have to pay more for equipment, commodities, and intermediate products from foreign markets.

2) **Social impact:**

- It will lead to decrease in standards of living as it will impact exports and economic growth impacting welfare of poor and their standard of lives.
- It will lead to rise in conflicts economically and politically.

3) **Political impact:** It would affect polity leading to instability in political framework of nations due to rise in prices and cost of living may lead to civil Uprisings.

4) **Impact on technology:** These tendencies limit technological advancement of the world as whole and of developing countries in particular. Limited knowledge

sharing, lack of flow of technology to developing countries limit advancement in science.

5) **Impact on environmental conversation:** Due to non-cooperation among nations it will impact environment conservation efforts in India. It will reduce required funding and would jeopardise efforts to conserve environment and tackle environment change. It would lead to lack of coordination at international organisation like UN where countries may not come at a common point to various problems like environmental change. It destroys the international order. This would impact India's interest which

6) **Impact on women employment:** De-globalisation would impact women empowerment efforts as it will impact women movements across the globe. Lack of coordination will reduce opportunities for women across the world.

7) **Impact on security:** Due to lack of coordination among various nations, security around the world along with India would impact. It will not only increase economic risks, but would provide an opportunity for terrorists to carry out violence due to lack of coordination among various law enforcement agencies.

8) **Impact on farmers:** A less coordinating world means impact in agricultural exports and Indian farmers. Indian farmers would face double whammy of environment change and de-globalisation.

Despite the critics view, the supporters say things may change very soon in the future. When developed countries like the United States and the United Kingdom take a step towards de-globalisation, other developing nations who look up to them may follow suit. Multiple factors are causing this shift from globalisation to de-globalisation. As economic power shifts from the Western to Asian nations, the U.S. and the U.K. have adopted self-protection policies. Rising security concerns and refuge crisis also play a role in creating support for de-globalisation.

15.6.5 Optimistic view of De-Globalisation

- **Developing local interest:** Walden Bello is among those who have noticed the emergence of the economic de-globalization process starting in 2004. He mentions the so-called “deconstruction”, later termed “de-globalization” in a pluralist world. In his opinion, de-globalization describes the means used by developing states in order to promote their local interests, at the cost of the ones endorsed by the supporters of globalization. The deglobalization process is not necessarily connected to the effects created by the economic or financial crises, but it may also be due to other causes (sharp drop in global demand, natural disasters, armed conflicts etc.). Globalisation is process is opposed to the process of increasing integration of markets and production, which does not only mean less global economy, but also more genuine cooperation between states.
- **Breaking the crises cycle:** Human resources like intellectual capital and material resources have to be taken into account. De-globalization does not necessarily express the manifestation of a destructive strategy dictated by the prolonged crisis faced by global capitalism but This also explains the sequence of several economic crises that have weakened the strength of globalization. Breaking the cycle means finding true alternatives to the current global system, with credible and accepting outcomes by all participants to the international trade in commodities and services.
- **Reconstruction Phase:** The de-globalization process is still in its initial phase. It will not end up in autarchy but in new national sovereignty. De-globalization thus becomes an effort of “reconstruction” which does not involve a withdrawal from the international economy, but its “reorientation”, capable of removing the deficiencies of globalized production, all the more so as the many facets of the actual system are fragile and unsustainable . Globalization has for some time become an inevitable phenomenon in the history of humanity. The last decades have been characterized by an enhancement of this phenomenon, due to unprecedented progress in technology, communications, science, transportation, biotechnologies, informatics, material production etc. The current stage of development of the world economy and

the evolution of contemporary capitalism transform de-globalization into a myth and not into an actual reality intended to impose itself as a driving force in the near future. Of course, globalization has brought forth advantages and disadvantages. It has allowed the cheapening of many products, it has vastly broadened markets and especially access to them, it has facilitated dissemination of new technologies, thus favouring economic growth

- **Individual economic strategy in accord with socio-cultural values** :

De-globalisation policies should be based on financial and technological agreements, to secure economic competitiveness of all countries. In the long run, unbalanced developments can generate intemperate enrichment of some nations, respectively the impoverishment of some others. Hence, de-globalization also means creating leeway so that each country can develop its own economic strategy in accordance with its cultural and social values, its economic necessities and possibilities of sustainable development.

15.5.6 Conclusion

De-globalisation has twin perspective it can have positive and negative impact economically, politically, socially and politically depending on the outlook and circumstances. Definitely we will be bereaved of all the benefits of globalisation including, less options, more cost, less employment opportunities but considering the geopolitical conflicts, disputes ,risk of terrorism, global financial crises, the path of de-globalisation is an alternative to protect local traders, restructuring , and ensuring global peace. Issues like Sino-Indian war between India and China, Covid-19 a virus supposedly from China, which has allegedly stopped the world economy and has brought health crises in the entire world, events like Pakistan frequent ceasefire violation, **U.S.** and **Iran** open **conflict** when the IRGC launched missile attacks against two Iraqi military bases housing **U.S.** soldiers in retaliation for the killing of Soleimani, a rare direct **Iran**–**U.S.** confrontation and the closest to the brink of war between the two nations in decades , Iran frequent threat to close Holmuz strait would affect many countries across globe which import oil. Such delicate happenings are raising war like situation at world level, hence de-globalisation is the required step which should be adopted for the time being to ensure worldwide peace.

15.7 CHECK YOUR PROGRESS

A) MULTIPLE CHOICE QUESTIONS

1) Contemporary Issues relate to-

a) Current issues

b) Historical events

c) Future challenges

d) None of the above

2) Contemporary marketing issues arise out of-

a) Changing socio-political environment

b) Changing economic environment

c) Changing environment

d) All of the above

3) Contemporary issues discussed in the chapter include-

a) Geopolitics

b) De-Globalization

c) Sustainable Development

d) All of the above

4) Regions vulnerability (climatic) depend on-

a) Infrastructure & Dependence on Agriculture

b) Population size

c) Government policies

d) None of the above

5) Trade related areas related to climate change?

a) Agriculture

b) Tourism

c) Trade

d) All of the above

B) Write true or false

1) Contemporary Issues arise due to dynamic environment?

2) Due to emerging marketing issues traditional marketing strategies should be readopted?

3) Food security means just economic access to food?

4) Sustainable Development denotes cutting down present needs foe future?

5) First Goal of Sustainable Development Goals is Zero Hunger?

C) Fill in the blanks

1) ------ means adopting policies which would reduce greenhouse gas ------ denotes diminishing negative impact of climate change

2) 4 pillars of food security are a) --- b) ---c) ---d) ---

3) WFP stands for-----

4) SDGs can be expanded as------

5) ------- explains disintegration among countries.

15.8 Summary

- **Need to Discuss Contemporary Issues**

Contemporary marketing issues arise out of radically changing worldwide economies. This has significantly transformed ways of marketing. As contemporary marketing issues are rising we find traditional marketing strategies unfit to the new framework and consequently companies are required to come up with novel ideas for synergetic interaction with existing and potential customers. Contemporary marketing concept is dynamic as we find speedily changing in marketing technology, environment, social, political and economic. Marketers who would build strategies in accord with the emerging issues in the surrounding environment would survive.

- **Contemporary Issue – Climate Change**

Climate change is one of the greatest challenges facing the international community. Mitigating global warming and adapting to its consequences will require major economic investment and, above all, unequivocal determination on the part of policy-makers. The long-term impacts of climate changes have been, temperature and sea level rises, and spike in extreme weather events, like wildfires and tropical storms, are critically affecting infrastructure, crop production, and the liveability of many heavily populated areas. Climate-related risks are also amplifying growing tensions stemming from trade, geopolitical, and domestic conflicts. Trade can effectively participate as a means of economic adaptation to climate change.

- **Contemporary Issue – Food Security**

Food Security means that all people every time have physical & economic access to adequate amounts of food which is nutritious, safe, and culturally appropriate foods, and is produced in an environmentally sustainable and socially just manner, moreover people are easily able to make informed decisions regarding food choices. Food Security also suggest that the people who are involved in food growing, producing, processing, transporting, retailing, and serving food are earning a decent wage. Market analysis in a food security context may provide tools for:

(i) planning food aid interventions with the assurance that their impact on local food production and food markets is not a negative one;

(ii) making the appropriate decision on whether cash/vouchers or food aid is the best suited option to address prevailing food insecurity; and

(iii) planning local or regional food purchases and ensuring that these are implemented at the optimal time with maximum developmental effect on domestic producers and markets

- **Contemporary Issue – Geopolitics**

Geopolitics is a method of studying foreign policy to understand and predict international political behaviour through different geographical variables. These include area studies, climate, topography, demography, natural resources, and applied science of the region which is being evaluated. Geopolitics focuses on political power related to geographic area. Geopolitical tensions have tremendous affect on marketing at national and international level as after globalisation inter country dependence has been increasing, like India import oil from Holmuz Strait and the passage has been creating conflicts due to hostile relation of Iran and America, Sino-India war, Pakistan constant ceasefire violations, Pakistan India trade was also affected after the surgical strike, fear of terrorism, US plan to block entry of Chinese airlines amidst the widespread pandemic, are among the current issues raising geopolitical tensions and they significantly affect trading at global level.

- **Contemporary Issues: Sustainable Development**

Sustainable development is development that meets the needs of the present without compromising the ability of future generations to meet their own needs. This means meeting the diverse needs of all people in existing and future communities, promoting personal wellbeing, social cohesion and inclusion, and creating equal opportunity. Sustainable development is about finding better ways of doing things, both for the future and the present. We might need to change the way we work and live now, but this doesn't mean our quality of life will be reduced right now. A sustainable development approach can bring many benefits in the short to medium term, for example: Health & Transport - Instead of driving, switching to walking or cycling for short journeys will save you money, improve your health and is often just as quick and convenient. Government is also intervening by various policies like ban on plastic, CSR policy and many other steps. Successful Indian Companies adopted Sustainable Development like Patanjali Ayurveda limited, Wipro Green Machines etc

- **Contemporary Issues – De-Globalization**

Deglobulisation has been regarded as a process of diminishing economic interdependence and integration between countries. De-globalisation has twin perspective it can have positive and negative impact economically, politically, socially and politically depending on the outlook and circumstances. Definitely we will be bereaved of all the benefits of globalisation including, less options, more cost, less employment opportunities but considering the geopolitical conflicts, disputes, risk of terrorism, global financial crises, the path of de-globalisation is the required step which should be adopted for the time being to ensure worldwide peace as we are witness geopolitical conflicts, food insecurity, global economy dwindling, International health crises, have created war like situations. Temporary cut off would help individual economy to design marketing policies to suit our socio-cultural behaviour, protect the domestic traders who were adversely affected from globalisation. As we have already seen dissolving of USSR, US withdrawal from Trans Pacific Free Trade Agreement, Britain disconnection from EU shows that countries want to serve their national interest first. All the contemporary issues are interrelated and together significantly shaping the business internal and external environment. Business people must keep close watch on the emerging issues at local and global level before formulating any business plan and before making any marketing strategy.

15.9 Key Words

Contemporary Issues, Climate Change, Global Warming, Adaptation and Mitigation, Food Security, Geopolitics, Sustainable Development, Sustainable Development Goals, De-Globalization

15.10 Self Assessment Test

Question 1 Explain business areas are vulnerable to Climate Change?

Question 2 What is Geopolitics? Throw light on current geopolitical challenges India is facing and how it would affect Indian marketing system?

Question 3 What are pillars of Sustainable Development? Illustrate Sustainable Development Goals?

Question 4 Globalisation was welcomed as new economic policy then why are countries moving towards De-Globalisation?

Question 5 Differentiate between Adaptation and Mitigation strategies? Which strategy would you suggest in India during Covid-19?

15.11 Answers To Check Your Progress

A) Multiple Choice Questions

1) a)

2) d)

3) d)

4) d)

5) Trade related areas related to climate change?

d) All of the above

B) Write true or false

1) True

2) False

3) False

4) False

5) False

C) Fill in the blanks

1) Mitigation, Adaptation

2) Availability, Accessibility, Utilization, Stability

3) World Food Programme

4) Sustainable Development Goals

5) De-Globalization

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Course: Business Environment	
Course Code: **MBA 105**	Author: **Dr. Rajiv Kumar**
Lesson No. **16**	Vetter: **Dr. Suresh K. Mittal**

Legislations For Social Responsibilities And Their Influences On Business Environment

STRUCTURE

16.0 Learning Objectives

After going through this lesson, the learner should be able to:

- Know about Consumer Protection Act, 1986
- Know about Competition Act, 2002
- Understand Environmental protection act, 1986

- Know about Foreign exchange Management Act, 1999

16.1 Consumer Protection Act, 1986

16.1.0 Introduction

Enactment of Consumer Protection Act, 1986 was one of the most important steps taken to protect the interests of the consumers. It was formulated after studying intensively the consumer protection act of a number of countries, and after through consultations with the representative of consumers, traders and industrialists.

16.1.1 Objectives

The major objectives and aims for the establishment of the Consumer Protection Act of 1986 are discussed below:

- Better protection of the interests or all consumers of any goods or services unless the governments specifically exempt.
- Establishment of consumer councils like the Central and State Consumer Protection Councils and the District Forum.
- Provision of better quality dispute redressal agencies that can help solve any dispute that arises between consumers and companies.
- Protection of the consumer rights.
- Protect consumers from exploitations or mistreatments.
- Ensure qualitative and effective consumer education. Consumers should be aware of their rights, their options and the solutions available at their disposal.
- An efficient platform for filing complaints of the consumers and solving the same.
- Attempting to provide a quality life for consumers.
- Teaching consumers and brands to live by ethical obligations and also gain genuine public support.

16.1.2 Applicability

All the provisions of the act come into force with the effect from 1st July, 1987. The act was thoroughly amended in 1991 and 1993. To make the consumer protection act more functional and purposeful, a comprehensive amendment 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.

16.1.3 Consumer Rights

In order for ensuring consumer protection, it is essential that every consumer know the basics of consumer protection. Discussed below are the fundamental consumer rights.

The right to be heard

Every consumer has the right to be heard after being exploited. An upset consumer should be aware that he/she possesses the right to take the matter to the authorities if the company does not hear them out. The right to be heard is a powerful right at the disposal of the consumer.

The right to seek redressal

Every consumer has the right to seek out for justice. Upset consumers who have been a victim of corporate exploitations can take the matter to the redressal agencies and file a suit against the insensitive company. This right is often put to ill use by many consumers and is hence a very delicate right.

The right to information

Every consumer has the right to information. Consumers should be amidst truthful genuine information. Information should not have an ill purpose and should not be incorrect. In other words, consumers have the right to truthful information.

The right of protection

Every consumer has the right of protection. Central Consumer Protection Council, State Consumer Protection Council, District Forum and Consumer Protection

Redressal Agencies are at the disposal of the consumers. These institutions aim at protecting Indian consumers from exploitative companies.

The right of assurance

Every consumer has the right of assurance -Assurance of qualitative goods and qualitative services. They also have the right to the assurance of the variety of commodities and services at their disposal.

The right of consumer education

Every consumer also has the right to receive consumer education. This education is often a part of every consumer protection act and amendment. The government should make immense effort to share and spread the consumer rights to every remote area of India. Consumers should also receive the right to get the education on the consumer do's and consumer don'ts. This is a very informative and knowledgeable right at the disposal of the consumers.

The right to a healthy environment

Every consumer has the right to be amidst a clean and healthy environment. Consumers have the right to purchase goods and services in a clean environment free from hassles and pressure. The consumer should not permit intense influence of any vendor because he/she is entitled to decide independently.

16.1.4 Consumer protection councils

The act provides for the establishment of a control consumer protection council by the central government and state consumer protection councils by the respective state government.

Consumer disputes redressal agencies

Section 9 of the consumer protection act provides for the establishment of a three-tier consumer disputed redressal system at the district, state and national level.

16.1.5 Three redressal agencies

1. A consumer disputed 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.

16.1.6 Composition of consumer redressal agencies

1. District forum: deals upto Rs. 20 lakh claims.
2. State commission: Deals claimed if any exceed Rs. 20 lakh but is not more than Rs. 1 crore.
3. National commission: Deals claimed exceeds Rs. 1 crore.

16.1.7 Remedial action

If any of the consumer redressal agencies is satisfied that the consumer suffer any of the defects they give an order to the opposite party to provide suitable remedies to the related person.

16.1.8 Appeal

1. If any person does not agree with the order of the district forum he may appeal against such order to the state commission within a period of 30 days from the date of the order (section 15).
2. If any person does not agreed with the order of state commission may prefer an appeal against such order to the national commission within a period of 30 day (section 19).

16.1.9 Penalties

According to section 27 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. 2000 but may extend to Rs. 10000 or with both.

16.1.10 Dismissal of Frivolous or Vexations complainant

Where a complainant found to be frivolous or vexations, 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.

16.1.11 Amendments in the Consumer Protection Act, 1986

The digital age has ushered in a new era of commerce and digital branding, as well as a new set of customer expectations. Digitization has provided easy access, a large variety of choice, convenient payment mechanisms, improved services and shopping as per convenience. However, along the growth path it also brought in challenges related to consumer protection. Keeping this in mind and to address the new set of challenges faced by consumers in the digital age, the Indian Parliament, on 6 August 2019, passed the landmark Consumer Protection Bill, 2019 which aims to provide the timely and effective administration and settlement of consumer disputes. The Consumer Protection Act, 2019 (New Act) received the assent of the President of India and was published in the official gazette on 9 August 2019. The New Act will come into force on such date as the Central Government may so notify. The New Act seeks to replace the more than 3 (three) decades old Consumer Protection Act, 1986 (Act).

Set out below are some of the key highlights of the new Act:

- **Covers E-Commerce Transactions:** The New Act has widened the definition of 'consumer'. The definition now includes any person who buys any goods, whether through offline or online transactions, electronic means, teleshopping, direct selling or multi-level marketing. The earlier Act did not specifically include e-commerce transactions, and this lacuna has been addressed by the New Act.

- **Enhancement of Pecuniary Jurisdiction:** Revised pecuniary limits have been fixed under the New Act. Accordingly, the district forum can now entertain consumer complaints where the value of goods or services paid does not exceed INR 10,000,000 (Indian Rupees Ten Million). The State Commission can entertain disputes where such value exceeds INR 10,000,000 (Indian Rupees Ten Million) but does not exceed INR 100,000,000 (Indian Rupees One Hundred Million), and the National Commission can exercise jurisdiction where such value exceeds INR 100,000,000 (INR One Hundred Million).
- **E-Filing of complaints:** The New Act provides flexibility to the consumer to file complaints with the jurisdictional consumer forum located at the place of residence or work of the consumer. This is unlike the current practice of filing it at the place of purchase or where the seller has its registered office address. The New Act also contains enabling provisions for consumers to file complaints electronically and for hearing and/or examining parties through video-conferencing. This is aimed to provide procedural ease and reduce inconvenience and harassment for the consumers.
- **Establishment of Central Consumer Protection Authority**: The New Act proposes the establishment of a regulatory authority known as the Central Consumer Protection Authority (CCPA), with wide powers of enforcement. The CCPA will have an investigation wing, headed by a Director-General, which may conduct inquiry or investigation into consumer law violations.

The CCPA has been granted wide powers to take suo-moto actions, recall products, order reimbursement of the price of goods/services, cancel licenses and file class action suits, if a consumer complaint affects more than 1 (one) individual.

- **Product liability & penal consequences**: The New Act has introduced the concept of product liability and brings within its scope, the product manufacturer, product service provider and product seller, for any claim for compensation. The term ‘product seller’ is defined to include a person who is involved in placing the product for a commercial purpose and as such would include e-commerce platforms as well. The defense that e-commerce platform merely act as ‘platforms’ or ‘aggregators’ will not be accepted. There are increased liability risks for manufacturers as compared to product service providers and product sellers, considering that under the New Act, manufacturers will be liable in product liability action even where he proves that he was not negligent or fraudulent in making the express warranty of a product. Certain exceptions have been provided under the New Act from liability claims, such as, that the product seller will not be liable where the product has been misused, altered or modified.

- **Unfair trade practices:** The New Act introduces a specific broad definition of Unfair Trade Practices, which also includes sharing of personal information given by the consumer in confidence, unless such disclosure is made in accordance with the provisions of any other law.
- **Penalties for misleading advertisement:** The CCPA may impose a penalty of up to INR 1,000,000 (Indian Rupees One Million) on a manufacturer or an endorser, for a false or misleading advertisement. The CCPA may also sentence them to imprisonment for up to 2 (two) years for the same. In case of a subsequent offence, the fine may extend to INR 5,000,000 (Indian Rupees Five Million) and imprisonment of up to 5 (five) years. The CCPA can also prohibit the endorser of a misleading advertisement from endorsing that particular product or service for a period of up to 1 (one) year. For every subsequent offence, the period of prohibition may extend to 3 (three) years.

The New Act fixes liability on endorsers considering that there have been numerous instances in the recent past where consumers have fallen prey to unfair trade practices under the influence of celebrities acting as brand ambassadors. In such cases, it becomes important for the endorser to take the onus and exercise due diligence to verify the veracity of the claims made in the advertisement to refute liability claims.

- **Provision for Alternate Dispute Resolution:** The New Act provides for mediation as an Alternate Dispute Resolution mechanism, making the process of dispute adjudication simpler and quicker. This will help with the speedier resolution of disputes and reduce pressure on consumer courts, who already have numerous cases pending before them.

With the New Act all set to become the law, gone are the days, where the 'consumer was asked to beware'. A consumer is now the one who assumes to be treated like a King. Hence, it is important for consumer driven businesses (such as, retail, e-commerce) to be mindful of the changes in the legal landscape and have robust policies dealing with consumer redressal in place. Consumer driven businesses must also strive to take extra precautions against unfair trade practices and unethical business practices.

16.2 Competition Act, 2002

16.2.0 Objectives

An Act, keeping in view of the economic development of the country, was laid down to provide for an establishment of a commission with the following objectives:

- To prevent practices having adverse effect on competition,
- To promote and sustain competition in markets,
- To protect the interests of consumers,
- To ensure freedom of trade carried on by other participants in markets in India and
- For matters connected there with or incidental there to.

16.2.1 Introduction

The competition act has been enacted to provide for the establishment of a commission to prevent practices having adverse effect on competition, to promote and sustain competition in market to protect the interests of consumers at large, and to ensure freedom of trade carried on by other participants in market in India, and for matters connected with or incidental thereto. With the coming into effect of the competition act, 2002 from September 1, 2009, the monopolies and restrictive trade practices (MRTP) act, 1969, was replaced and later the MRTP commission was replaced by competition commission of India (CCI).

16.2.2 Features of Competition Act, 2002

The focus of the new law is towards the following areas affecting competition namely:

1. Prohibition of certain agreements, which are considered to be anti competitive in nature. Such agreements [namely tie in arrangements, exclusive dealings (supply and distribution), refusal to deal and resale price maintenance] shall be presumed as anti-competitive if they cause or are likely to cause an appreciable adverse effect on competition within India.

2. Prohibition of abuse of dominant position- If an enterprise by imposing unfair or discriminatory conditions or limiting and restricting production of goods or services or indulging in practices resulting in denial of market access or through in any other mode are prohibited.

3. Regulation of combinations which cause or are likely to cause an appreciable adverse affect on competition within the relevant market in India is also considered to be void.

4. Entrust Competition Commission of India the responsibility of undertaking competition advocacy, awareness and training about competition issues.

16.2.3 Definitions

Acquisition [Section 2(a)]

"Acquisition" means, directly or indirectly, acquiring or agreeing to acquire—

(i) Shares, voting rights or assets of any enterprise; or

(ii) Control over management or control over assets of any enterprise;

Agreement [Section 2(b)]

"Agreement" includes any arrangement or understanding or action in concert,

(i) Whether or not, such arrangement, understanding or action is formal or in writing; or

(ii) Whether or not such arrangement, understanding or action is intended to be enforceable by legal proceedings;

Cartel [Section 2(c)]

"Cartel" includes an association of producers, sellers, distributors, traders or service providers who, by agreement amongst themselves, limit, control or attempt to control

The production, distribution, sale or price of, or, trade in goods or provision of services.

16.2.4 Main provisions

1. Prohibits anti-competitive agreements.
2. Prohibits abusive behavior of a dominant firm.
3. Regulates mergers and acquisitions.
4. Mandates competition advocacy.

16.2.5 Competition commission and competition appellate tribunal

The competition commission of India (CCI), established under the competition act, consisting of a chairperson and six members, became functional with effect from 1st March 2009.

16.2.5.0 Anti- competitive agreements

The act prohibits agreements in respect of production, supply, distribution, storage, acquisition or control of goods or provision of services which causes or is likely to cause an appreciable adverse effect on competition within India.

According to the act, agreement or decisions which have any of the following effects shall be presumed to have appreciable adverse effect on competition:

a) Directly or indirectly determining purchase or sale prices.

b) Limiting or controlling production, supply, markets, technical development, investment or provision of services.

c) Directly or indirectly resulting in bid rigging or collusive bidding, shall be presumed to have an appreciable adverse effect on competition.

16.2.5.1 Abuse of dominant position

Section 4 of the competition act lays that no enterprise shall abuse its dominant position. Dominant position means a position of strength, enjoyed by an enterprise, in the relevant market in India which enables it to:

- Operate independently of competitive forces prevailing in the relevant market
- Affect its competitors or consumers or the relevant market in its favors

16.2.5.2 Regulations of combinations

Under the Competition Act 2002, the regulation of combinations means the acquisition of one or more enterprises in the market by one or more person through a merger or amalgamation of enterprises where -

- The parties to acquisition, whose control, shares, voting rights or assets have been acquired or being acquired jointly, be it either in India or outside India.

- The Group to which the enterprise whose control, shares, assets or voting rights have been acquired or being acquired after the acquisition is either in India (with assets of value more than four thousand crores or turnover of more than twelve thousand crores), or outside India (with assets of value more than two billion US Dollars or of turnover more than six billion US dollars).

- Acquisition of control by a person over an enterprise when such person already have direct or indirect control of another such enterprise which is engaged in the production, distribution, trading of a similar or identical or substitutable goods or services, the enterprise over which the control has been acquired along with the enterprise which is already in control of the acquirer, be it in India (of assets more than one thousand crore or turnover more than three thousand crores), or outside India (of value more than five hundred million US dollars or turnover more than fifteen million US dollars).

No person shall enter such a combination which may cause or is likely to cause appreciable adverse effect on the competition within the relevant market in India and all such combination shall be deemed void under the provisions of the Competition Act 2002.

16.2.6 Power to exempt

a) Any class of enterprises if such exemption is necessary in the interest of security of the state or public interest.

b) Any practice or agreement arising out of and in accordance with any obligation assumed by India under any treaty, agreement or convention with any other country or countries.

c) Any enterprise which performs a sovereign function on behalf of the central government or a state government, provided that in case an enterprise is engaged in any activity including the activity relatable to the sovereign functions of the government, the central government may grant exemption only in respect of activity relatable to the sovereign functions.

16.2.7 Amendments in Competition Act, 2002

The Competition Commission of India (CCI) has constantly reformed the merger control regulations from 2011. In 2018, the CCI took it upon itself to further streamline the merger control regime to increase the ease of doing business in India. The pro-active effort which the CCI initiated last year has matured as it notified its 7th set of amendments (Amendment Regulations 2019) to the Competition Commission of India (Procedure in regard to the transaction of business relating to combinations) Regulations, 2011 (Combination Regulations). In essence, the Amendment Regulations 2019 appear to be a culmination of enduring deliberations with the Ministry of Corporate Affairs (MCA) over the last few months to further ease the approval process for mergers and acquisitions in India. The Amendment Regulations 2019 will be effective from 15 August 2019.

Given the significant shift brought by the Amendment Regulations 2019 in the merger control regime, this update endeavours to highlight the salient features of the latest amendments, including their practical implications on domestic and foreign clients.

The Amendment Regulations 2019 are set out below:

- A green channel mechanism has been introduced which can be optionally utilized by parties to certain types of transactions set out in the newly added Schedule III to the Combination Regulations (discussed below).
- Upon receipt of an acknowledgment of a notification filed under the green channel, the transaction will be deemed approved.
- The notification, which is designed as an automatic approval channel, will need to be accompanied by a declaration set out in Schedule IV of the Combination Regulations.
- Schedule III stipulates that the green channel route will be available to the parties which do not have any horizontal, vertical or complementary overlaps. While determining overlaps, parties are now formally required to consider all plausible alternative relevant market definitions. The overlaps also need to be evaluated vis-à-vis: (i) the parties themselves, (ii) all the group entities for all the parties, (iii) all entities where the parties directly or indirectly hold shares, and (iv) all entities where the parties directly or indirectly exercise control.
- If the CCI determines that a transaction does not fall within the scope of Schedule III and the declaration under Schedule IV is found to be incorrect, then the deemed approval shall be void ab initio and the CCI shall deal with the combination in accordance with the provisions of the Competition Act, 2002 (Act).

- However, prior to deciding if the notification is void ab initio, the CCI will afford the parties an opportunity of being heard.

Practical Implications

- The idea of a green channel mechanism is certainly laudable to further the ease of doing business in India. This will permit the CCI to prioritize its resources. However, there is a danger that the mechanism will be rendered ineffective given its narrow scope of applicability and uncertainties surrounding its structure.
- Schedule III requires parties to ensure that there are no horizontal, vertical or complementary overlaps in all plausible alterative market definitions. The incorporation of this expression has far reaching ramifications and makes an overlap assessment highly onerous in application. The assessment will now need to be run for all possible alternative market definitions which makes the entire exercise very burdensome and may limit the exercise of this option.
- Complementary activity is a newly introduced expression and there is no guidance on the import or interpretation of complementary activities. This again places a heavy burden on parties to determine what constitutes complementary activity and may require the parties to effectively seek the CCI's views through informal consultations, on a case by case basis. Further, given the onus imposed on the parties, even assessing suitable horizontal and vertical overlaps to the CCI's satisfaction may turn out to be challenging.
- The overarching language of Schedule III requires ascertaining overlaps between group entities of both acquirer and target (including all entities in which both the parties directly and indirectly hold shares). Given that the target group outside the "true" target (ie, entity, business or asset actually being acquired) will not be part of the post transaction acquirer group, this requirement seems out of place and onerous.

- Further in practice, identifying all the entities in which each, the acquirer and the target, have direct or indirect shareholding would be a burdensome task, more specifically for identifying minor shareholding in listed companies. Pure financial investors including private equity funds may be deeply affected by this requirement.

- The Amendment Regulations 2019 also do not specify the actions that will follow if the merger notification is declared void ab initio. For example, whether another notification would be required, how would the CCI assess the transaction etc. Under the current framework, when a merger notification is invalidated by the CCI, the Combination Regulations set out the way forward. Given the absence of clarity in the Amendment Regulations 2019, parties may be looking at uncertain consequences for making an involuntary misstep.

Potential legislative issues

- The Act does not contemplate a deemed approval mechanism. As such, Section 6(2A) specifically provides that a combination will not come into effect either before the CCI has approved the same by way of an order, or 210 (two hundred and ten) days have passed from the date the notice was filed.

- The requirement of an order under Section 31 seems to require the CCI's assessment prior to approval of a transaction. In this regard, risks always remain on whether the deemed approval process will squarely fall under the scope of Section 6(2A).

- Given that the Act does not contemplate the possibility of a deemed approval unless it is due to lapse of the prescribed timeframe, the validity of the Amendment Regulations 2019 is prone to a challenge as the Combination Regulations being a delegated legislation ought not to expand the scope of the legislative intent under Section 6(2A), particularly when it would appear to be contrary to the parent enactment.

Amendment to the Structure of Form I

- The Amendment Regulations 2019 have restructured Form I to introduce certain additional items. It now requires details of:
  - inter-connected transactions;
  - rights acquired by the parties to the combination;
  - foreign investment as a result of the combination;
  - information on complementary business activities between the parties, etc.; market-facing data (such as, market size, shares and competitor/customer/supplier information) for the last 3 (three) years as against the current practice of the last 1 (one) year; all plausible alternative relevant markets (including explanations for accepting or rejecting a specific definition); and any proceedings before the CCI or other competition authority(ies) to which they are/were a part of in the last 5 (five) years.
- The CCI has further streamlined the structure of Form I based on its learnings over the years.
- The burden on the parties to choose and justify their choice of relevant market definition is greatly increased. This intent extends to the heavy data-gathering exercise for market information which is now required for the preceding 3 (three) years, regardless of the extent of overlaps.
- It may be noted that the requisition from the transacting parties for competition law related proceedings for last 5 years is a part of Form II merger notification. The same has now been introduced in the revised Form I and as such, will act as an additional disclosure/ compliance item for the transacting parties.

Amendment to the Public Summary Mechanism

- Previously, a merger notification was required to be accompanied with a long summary and a short summary. The short summary was uploaded on the website of the CCI for public access. The Amendment Regulations 2019 have done away with the requirement of 2 (two) summaries.

- The parties are now required to submit only 1 (one) summary (below 1000 (one thousand) words) with information on: (i) name of the parties, (ii) nature and purpose of the combination, (iii) products/services or businesses of the parties, and (iv) the markets in which the parties operate. This summary will also be published by the CCI on its website.

16.3 The Environment (Protection) Act, 1986

16.3.0 Objectives

- To protect and improve air, water and land environment.
- To prevent hazards to all living creatures and properties.
- To maintain a pleasant relationship between human being and their environment.

16.3.1 Introduction

The environment (protection) act was enacted in the year 1986 with the main objective to provide the protection and improvement of environment and for matters connected therewith. The act is one of the most comprehensive legislations with pretext to protection and improvement of environment.

On a cold wintery midnight in December 1984 when the city of Bhopal was sound asleep and the workers at Union Carbide India Ltd. pesticide plant were completing their routinely task, t no one was aware about the tragedy that was about to strike the city. Suddenly, the families and workers living in the vicinity woke up to sound of emergency alarm bell and repugnan smell that filled the air making it difficult for the local population to breath. By the morning, more than thousand people had already died due to the gas leak that took place inside UCIL plant and spread in the atmosphere. The Methyl isocyanate (MIC) gas in the atmosphere exposed people to severe irritation in the eyes, coughing, blepharospasm, and burning sensation within the respiratory tracts. Till now, families are suffering because of the horrors committed by UCIL with more than 500,000 people affected, while owners fled the scene due to weak environmental and civil laws.

The Constitution of India also provides for the protection of the environment. Article 48A of the Constitution specifies that the State shall endeavor to protect and improve the environment and to safeguard the forests and wildlife of the country. Article 51 A further provides that every citizen shall protect the environment.

16.3.2 The watershed moment that led to the formulation of EPA

Bhopal Gas Tragedy considered the worst industrial disaster in the world was a watershed moment for India and country's Parliament, as the lawmakers gathered to formulate stronger norms, acts, policies, and laws to ensure that such horrific incidents do not occur in India again. The Environment Protection Act of 1986 (EPA) was enacted by the Government of India under Article 253 of the Indian Constitution. The Act came in as a result of the Bhopal gas tragedy as well as India's commitment to follow United Nations Conference on the Human Environment that took place at Stockholm in June, 1972. The conference was attended by 122 nations that passed the Stockholm Declaration that contained 26 principles that focused on development, environment, and the necessity of human interaction with the environment. The aim of the Environment Protection Act of 1986 is to improve and protect the human environment, most importantly to prevent hazards from happening and causing damage to the ecology.

16.3.3 Important features of this act

1. This act empowers the government to lay down procedures and safeguards for prevention of accidents that cause pollutions and remedial measures of an accident occur.
2. The government has the authority to close or regulate any industry or its operation if violation of the provision of the act occurs.

3. Any person who fails to comply or contravenes any provision of the act is punishable with imprisonment for a term extending upto five years or a fine upto one lakh rupees or both.
4. An additional fine of Rs. 5,000 per day may be imposed for entire period of violation of rules.
5. The act fixes the liability on the person who is directly in-charge unless it is proved that the offence was committed without his/her knowledge or consent.
6. This act empowers the officer of central government to inspect the site and collect samples of air, water, soil or other material for testing.

This act is the most comprehensive legislation with powers for central government to act directly without interference from regulatory authorities or agencies.

16.3.4 Definitions

Section 2 of the EPA deals with the definitions given below. Some important definitions provided in the Section are:

- Section 2 (a) "**Environment**" includes water, air, and land and the interrelationship that exists among and between water, air and land and human beings, other living creatures, plants, micro-organism and property. This definition is not exhaustive but an inclusive one.
- Section 2 (b) "**Environmental Pollutant**" means any solid, liquid or gaseous substance present in such concentration as may be, or tend to be injurious to environment.
- Section 2 (c) "**Environmental Pollution**" means the presence in the environment of any environmental pollutant. This implies an imbalance in the environment. The materials or substances when after mixing in air, water or land alters their properties in such manner, that the very use of all or any of the air-water and land by man and any other living organism becomes lethal and dangerous for health.

- Section 2 (e) "**Hazardous Substance**" means any substance or preparation which, by reasons of its chemical or Physico-chemical properties or handling, is liable to cause harm to human beings, other living creatures, plants, micro-organism, property or environment.

16.3.5 Who can make the complaint?

A complaint under this act can be made by the Central government or any other authority by that government or, any person who has given notice of not less than 60 days of the alleged offence and of his intention to make complaint to the central government or the authorized officer.

16.3.6 Powers of Central Government to take measures to protect and improve environment

According to the provisions of the Act, the Central Government shall have the power to take all such measures as it deems necessary or expedient for the purpose of protecting and improving the quality of the environment and preventing controlling and abating environmental pollution.

Such measures may include measures with respect to all or any of the following matters, namely:

- co-ordination of actions by the State Governments, officers and other authorities- (a) under this Act, or the rules made there under, or (b) under any other law for the time being in force which is relatable to the objects of this Act;
- planning and execution of a nation-wide programme for the prevention, control and abatement of environmental pollution;
- laying down standards for the quality of the environment in its various aspects;

- laying down standards for emission or discharge of environmental pollutants from various sources whatsoever: Provided that different standards for emission or discharge may be laid down under this clause from different sources having regard to the quality or composition of the emission or discharge of environmental pollutants from such sources;
- restriction of areas in which any industries, operations or processes or class of industries, operations or processes shall not be carried out or shall be carried out subject to certain safeguards;
- laying down procedures and safeguards for the prevention of accidents which may cause environmental pollution and remedial measures for such accidents;
- laying down procedures and safeguards for the handling of hazardous substances;
- examination of such manufacturing processes, materials and substances as are likely to cause environmental pollution;
- carrying out and sponsoring investigations and research relating to problems of environmental pollution;
- inspection of any premises, plant, equipment, machinery, manufacturing or other processes, materials or substances and giving, by order, of such directions to such authorities, officers or persons as it may consider necessary to take steps for the prevention, control and abatement of environmental pollution;
- establishment or recognition of environmental laboratories and institutes to carry out the functions entrusted to such environmental laboratories and institutes under this Act;
- collection and dissemination of information in respect of matters relating to environmental pollution;

- preparation of manuals, codes or guides relating to the prevention, control and abatement of environmental pollution;
- such other matters as the Central Government deems necessary or expedient for the purpose of securing the effective implementation of the provisions of this Act.

The Central Government may, if it considers it necessary or expedient so to do for the purpose of this Act, by order, published in the Official Gazette, constitute an authority or authorities by such name or names as may be specified in the order for the purpose of exercising and performing such of the powers and functions (including the power to issue directions under section (5) of the Central Government under this Act.

And for taking measures with respect to such of the matters referred to in sub-section (2) as may be mentioned in the order and subject to the supervision and control of the Central Government and the provisions of such order, such authority or authorities may exercise any powers or perform the functions or take the measures so mentioned in the order as if such authority or authorities had been empowered by this Act to exercise those powers or perform those functions or take such measures. This can be achieved only by careful assessment of a project proposed to be located in any area, on the basis of an environmental impact assessment and environmental management plan for the prevention, elimination or mitigation of the adverse impacts, right from the inception stage of the project.

The Central Government has passed certain notifications laying that the expansion or modernization of any existing industry or new projects listed shall not be undertaken in any part of India unless it gets environmental clearance by the Central Government or the State Government.

16.3.7 Powers of the Court

The Act does not curtail the powers of the Supreme Court. It has from time to time in various matters issued directions and orders to control pollution. Some such important cases pertaining to the protection of the environment are:

- **Directions issued to control vehicular pollution**

In **Mehta v. Union of India (1998) 6 SCC 63**, in order to control the chaotic traffic conditions and vehicular pollution, the Supreme Court issued the following directions. All commercial/transport vehicles which are more than 20 years old should be phased out and not permitted to ply in Delhi after October 1998. All such commercial /transport vehicles which are 17 to 19 years old (3200) shall not be permitted to ply in the National Capital Territory, Delhi after 1998. Such of the commercial /transport vehicles which are 15 and 16 years old (4962) shall not be permitted to ply after December 31, 1998. The Supreme Court made this order applies to all commercial/transport vehicles whether registered in the National Capital Territory of Delhi or outside (but ply in Delhi) which are of more than stipulated age and which do not have any authority to ply in Delhi.

- **Protection of Coastline of India**

In Indian Council for Enviro-Legal Action v Union of India (1996 AIR 1446), the Supreme Court in regard to the 600 km long coastline emphasized that it would be the duty and responsibility of the coastal states and Union Territories in which the stretch exists, to see that the notifications issued, declaring the coastal stretches should be properly and duly implemented.

Further, the various restrictions on the setting up and expansion of industries, operation or process, etc. in the regulation Zone should be strictly enforced.

Under this principle, it is not the role of the Government to meet the costs involved in either prevention of such damage or in carrying out remedial action, because the effect of this would be to shift the financial burden of the pollution incident on the taxpayer. The responsibility of repairing the damage is that of the offending industry.

16.3.8 Penalties

1. Sec. 15 of the EPA provides that any person who fails to comply or contravenes any of the provisions of the act, or the rules made or orders or directions issued under the act or rules, than for such failure or contravention, he shall be punishable:

a) With imprisonment for a term which may extend to 5 years

b) With fine which may extend to one lakh rupees

c) With both

2. On case the failure or contravention after the conviction for first failure or contravention, an additional fine which may extend to Rs. 5000 per every day can be imposed for a period during which failure or contravention continues.

3. If the failure or contravention continues beyond a period of one year after conviction, the offender shall be punishable with imprisonment for a term which may extend to seven years.

16.3.9 Conclusion

In conclusion, environment pollution is affecting not only individual but also entire countries all over the world. The awareness towards improving the quality of environment has increased substantially and all efforts are being made at different levels to minimize environment pollution and thus help in improving the quality of life.

16.4 Foreign Exchange Management Act (FEMA), 1999

16.4.0 Objectives of FEMA

The main objective of FEMA was to help facilitate external trade and payments in India. It was also meant to help orderly development and maintenance of foreign exchange market in India. It defines the procedures, formalities, dealings of all foreign exchange transactions in India. These transactions are mainly classified under two categories -- Current Account Transactions and Capital Account Transactions.

FEMA is applicable to all parts of India and was primarily formulated to utilize the foreign exchange resources in efficient manner. It is also equally applicable to the offices and agencies which are located outside India however is managed or owned by an Indian Citizen. FEMA head office is known as Enforcement Directorate and is situated in heart of city of Delhi.

16.4.1 Foreign exchange management (FEMA), 1999

FEMA, 1999 was replaced foreign exchange regulation act, 1973 (FERA) with effect from June 1, 2000. The replacement was a great sigh of relief for the people as FERA was unduly stringent in its criminal provisions. FEMA is a civil law and proactive in its outlook compared to FERA. The thrust of FEMA is to manage the scare foreign exchange resources of the country rather than to control them as was prevalent under FERA. FEMA met the need of the day in the changed economic scenario of India, especially since 1999.

i. It is consistent with full current account convertibility and contains provisions for progressive liberalization of capital account transactions.

ii. It is more transparent in its application as it lays down the areas requiring specific permissions of the Reserve Bank/Government of India on acquisition/holding of foreign exchange.

iii. It classified the foreign exchange transactions in two categories, viz. capital account and current account transactions.

iv. It provides power to the Reserve Bank for specifying, in , consultation with the central government, the classes of capital account transactions and limits to which exchange is admissible for such transactions.

v. It gives full freedom to a person resident in India, who was earlier resident outside India, to hold/own/transfer any foreign security/immovable property situated outside India and acquired when s/he was resident.

vi. This act is a civil law and the contraventions of the Act provide for arrest only in exceptional cases.

vii. FEMA does not apply to Indian citizen's resident outside India.

16.4.2 Regulations of foreign exchange transactions

Foreign exchange transactions were regulated in India by the foreign exchange regulations act (FERA), 1973. This act also sought to regulate certain aspects of the conduct of business outside the country by Indian companies and in India by foreign companies.

The Reserve Bank can, by regulations, prohibit, restrict or regulate the following• transfer or issue of any foreign security by a person resident in India;

• transfer or issue of any security by a person resident outside India;

• transfer or issue of any security or foreign security by any branch, office or agency in India of a person resident outside India;

• any borrowing or lending in foreign exchange in whatever form or by whatever name called;

• any borrowing or tending in rupees in whatever form or by whatever name called Between a person resident in India and a person resident outside India;

• deposits between persons resident in India and persons resident outside India;

• export, import or holding of currency or currency notes;

• transfer of immovable property outside India, other than a lease not exceeding five years, by a person resident in India;

• acquisition or transfer of immovable property in India, other than a lease not exceeding five years, by a person resident outside India;

• giving of a guarantee or surety in respect of any debt, obligation or other liability Incurred

(i) By a person resident in India and owed to a person resident outside India or

(ii) By a person resident outside India.

A person, resident in India may hold, own, transfer or invest in foreign currency, foreign security or any immovable property situated outside India if such currency, security or property was acquired, held or owned by such person when he was resident outside India or inherited from a person who was resident outside India.

A person resident outside India may hold, own, transfer or invest in Indian currency, security or any immovable property situated in India if such currency, security or property was acquired, held or owned by such person when he was resident in India or inherited from a person who was resident in India.

16.4.3 Applicability of FEMA

FEMA is applicable to the whole of India. The expression whole of India would indicate that the provisions of the act are applicable to all transactions that are taking place in India. Thus, any person who is present in India at the time of transaction has to comply with the provisions of FEMA. FEMA is applicable to all branches, offices, and agencies outside India that are owned or controlled by a PRI. Thus, FEMA has retained its extra territorial jurisdiction as under FERA.

16.4.4 Important definitions

1. Holding of foreign exchange
2. Current account transactions
3. Capital account transactions
4. Export of goods and service

16.4.5 Realization and repatriation of foreign exchange

Where any amount of foreign exchange is due or has accrued to any PRI, such person shall take all reasonable steps to realize and repatriate to India such foreign exchange within such period and in such manner as may be specified by the reserve bank.

Exemption from realization and repatriation is granted in certain cases where RBI sets up the limits and the transactions are complaint with the same.

16.4.6 Administration of the Act

The FEMA has assigned an important role to the reserve bank of India in the administration of this act. The rules, regulations and norms pertaining to several sections of the act are to be laid down by the RBI, in consultation with the central government.

The act requires the central government to appoint as many officers of the central government as adjudicating authorities for holding inquiries pertaining to contravention of the act.

16.4.7 Authorities and Enforcement Machinery

FEMA in itself is not an independent and isolated law. The provisions of FEMA are spread at different place and so there are regulatory bodies. Reserve Bank of India makes Regulations for FEMA and the Rules are made by Central Government.

Authorities governing the enforcement of FEMA are:

1. Foreign Exchange Department of Reserve Bank of India.

2. Directorate of Enforcement, Department of Revenue, Ministry of Finance.

3. Capital Market Division, Department of Economic Affairs, Ministry of Finance.

4. Foreign Trade Division, Department of Economic Affairs, Ministry of Finance.

16.4.8 Machinery responsible for various aspect of FEMA

1. Enforcement Directorate: To investigate provisions of the Act, the Central Government, have established the Directorate of Enforcement with Directors and other officers as officers of the Enforcement.

2. Adjudicating Authorities: The Adjudicating Authorities will issue a notice to the person who has contravened the provisions of the Foreign Exchange Management Act, rules, regulations, notifications or any directions issued by the RBI.

3. Special Director (Appeals): Any person aggrieved by an order made by the Adjudicating Authority, being an Assistant Director of Enforcement or a Deputy Director of Enforcement can prefer an appeal to the Special Director (Appeals).

4. Appellate Tribunal: Any person aggrieved by an order made by the adjudicating Authority, or the Special Director (Appeals) can prefer an appeal to the Appellate Tribunal. FEMA envisages that RBI shall have controlling role in management of foreign exchange. Since RBI cannot directly handle foreign exchange transactions, it authorizes "Authorised Persons" to deal in foreign exchange as per direction issued by RBI.RBI is empowered to issue direction to such "Authorized Persons". These Directions are issued through AP (DIR) Circulars (AP stand for Authorized Person and DIR stand for Directions).

The Ministry of Finance (Department of Economic Affairs) has notified the Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 dated 17 October 2019 (**Principal Rules**) in supersession of erstwhile Foreign Exchange Management (Transfer of Issue of Security by a Person Resident outside India) Regulations, 2017 and the Foreign Exchange Management (Acquisition and Transfer of Immovable Property in India) Regulations, 2018.

16.4.9 An Overview of Amendments

The Ministry of Finance has come out with amendment notification, i.e. Foreign Exchange Management (Non debt Instruments) (Second Amendment) Rules, 2020 S.O. 1374(E).dated 27th April, 2020, (Amended Rules) which inter-alia include:

- Acquisition after renunciation of rights;
- Applicability of sourcing norms on Single brand retail trading;

- 100% investment under automatic route in Intermediaries or insurance intermediaries, subject conditions;
- Divestment by foreign Portfolio Investor (FPI) under conditions as prescribed by SEBI.

Acquisition by a person resident outside India (PROI) after renunciation of rights by other shareholder

Insertion of new rule 7A which inter-alia states that whenever a PROI acquired a right towards offered shares from a person resident in India (who has renounced it), may acquire equity instruments of an Indian Company (other than share warrants)by exercising such right subject to pricing guidelines specified under Principal Rules.

It is pertinent to state here that under the Principal Rules, there was an explanation to Rule 7 which laid down that the conditions specified in Rule 7 are also applicable in case a non-resident made an investment in the equity instruments (other than share warrants) pursuant to exercise of right renounced by the person to whom it was offered. These conditions inter-alia states that: Offer made by the India company should be compliance of the Companies Act, 2013, compliance of sectoral cap, as applicable, the existing shares pursuant to which shares have been offered, should have issued in compliance Principal Rules, pricing conditions for listed company as well unlisted company.

Now, the amendment rules has deleted the aforesaid explanation appended to Rule 7, and rule 7A has been inserted, resultant, non-resident can now subscribe to renounced shares in a rights issue, which have been renounced by a resident in its favour, subject to the pricing guidelines prescribed under the Principal Rules.

Applicability of sourcing norms on Single Brand Retail Trading

Amendment in the Principal Rules, in Schedule 1, in the Table, which read as: Pursuant to the stated amendment the period from which the sourcing norm would become applicable would be 3 years from commencement of the first store or start of online retail, whichever is earlier.

In the Principal Rules, before the amendment, said period for applicability of sourcing norms was 3 years from the commencement of business which meant opening of the first store by such entity engaged in single brand retail trading of such products having ‘state-of-art’ and ‘cutting-edge’ technology and where local sourcing is not possible.

100% FDI in Intermediaries or insurance intermediaries

In line with the 2019/20 budget presented on 5 July 2019 and amendment in Indian Insurance Companies (Foreign Investment) Rules, 2015, dated 2nd September 2019, limit of foreign direct investment in insurance intermediaries increased to 100% from previous limit of 49%, aligning with the budget and stated amendment, the Department of Economic Affairs has amended the Principal Rules. Accordingly, now the intermediaries or insurance intermediaries including insurance brokers, reinsurance brokers, insurance consultants, corporate agents, third party administrators, surveyors, loss assessors, and such other entities as may be notified by the Insurance Regulatory and Development Authority of India (IRDAI) would be eligible to receive 100% FDI under the automatic route subject to fulfillment of appended conditions.

Further to this if an insurance intermediary that has majority shareholding of foreign investors shall undertake the following:

- To be incorporated as a limited company under the provisions of the Companies Act, 2013;
- At least one from among the Chairman of the Board of Directors or the Chief Executive Officer or Principal Officer or Managing Director of the insurance intermediary shall be a resident Indian citizen;

- Such insurance intermediaries are not permitted to make payments to a foreign group or promoter or subsidiary or interconnected or associate entities beyond the limits prescribed by the IRDAI.
- The intermediaries are to make relevant disclosures in the prescribed format; and
- They are required to bring in the latest technological, managerial and other skills.

Divestment by Foreign Portfolio Investor (FPI), subject to further conditions as prescribed by SEBI

In case of breach of investment limits by an FPI, the divestment of holdings by the FPI and the reclassification of FPI investment as foreign direct investment shall be subject to further conditions, if any, specified by the Securities and Exchange Board of India and RBI, in this regard.

Key consideration: Rule 7 itself state that price in case of rights issue to persons resident outside India shall be a price determined by the company and in case of an unlisted Indian company, it shall not be at a price less than the price offered to persons resident in India, however, by virtue of Rule 7A bringing additional pricing condition as specified under rule 21 applicable on acquisition of shares by exercising the renounced right , there would be duel pricing provisions applicable. Further, this notification has been issued by Department of Economic Affairs with an intent to ensure ease of doing business, however, compliance of numerous additional conditions by insurance intermediary in case it has majority shareholding of foreign investors (foreign owned and control entity). Also, unwanted restrictions on payments to be made to related parties, repatriation of dividends, board composition etc. on such insurance intermediary would deteriorating frequent FDI in such entities.

16.4.10 FERA and FEMA – A Comparison

- In FEMA, only the specified acts relating to foreign exchange are regulated while in FERA, anything and everything that has to do with foreign exchange was controlled.
- FEMA is a much smaller enactment –only 49 sections as against 81 of FERA.
- In the process of simplification, many of the laid down of the erstwhile FERA have been withdrawn.
- Many provisions of FERA likes the ones relating to blocked accounts, Indians taking up employment abroad, employment of foreign technicians in India, contracts in evasion of the act, vexatious search, culpable mental state etc., have no appearance in FEMA.

16.5 Check Your Progress

Multiple choice questions

1. Which of the following is the objective of Consumer protection act, 1986?

a. Protection of the consumer rights.

b. An efficient platform for filing complaints of the consumers and solving the same.

c. Attempting to provide a quality life for consumers.

d. All of the above

2. Which of the following is the right of the consumers?

a. Right to be heard

b. Right to information

c. Both a and b

d. None of the above

3. District forum: deals up to __________.

a. Rs. 20 lakh claims

b. exceed Rs. 20 lakh but is not more than Rs. 1 crore

c. exceeds Rs. 1 crore

d. None of the above

4. State commission deals claimed ________.

a. Rs. 20 lack claims

b. exceed Rs. 20 lack but is not more than Rs. 1 crore

c. exceeds Rs. 1 crore

d. None of the above

5. National commission deals claimed ________.

a. Rs. 20 lack claims

b. exceed Rs. 20 lack but is not more than Rs. 1 crore

c. exceeds Rs. 1 crore

d. None of the above

6. MRTP act 1969 replaced by ________.

a. Consumer protection act 1986

b. Competition act, 2002

c. Environmental protection act, 1986

d. FEMA act, 1999

7. CCI stands for ________.

a. Competition commission of India

b. Contract committee of India

c. Commercial commission of India

d. Competition Committee of India

8. The environment protection act was enacted in the year ________.

a. 1975

b. 1986

c. 1990

d. 1999

9. Which of the following is the objective of Environment protection act, 1986?

a. To protect and improve air, water and land environment.

b. To prevent hazards to all living creatures and properties.

c. To maintain a pleasant relationship between human being and their environment.

d. All of the above

10. The main objective of ____________ was to help facilitate development and maintenance of foreign exchange market in India.

a. FEMA act, 1999

b. MRTP act,1969

c. COPRA act, 1986

d. Competition act, 2002

16.6 Summary

The chapter is based on legal legislations for social responsibilities and their influences on business environment focused on consumer protection act 1986, competition act 2002, FEMA 1999 and environmental protection act 1986 with their objectives and provisions. All acts have been discussed in the Indian perspectives with their relevance and significance for business and society. Enactment of consumer protection act, 1986 was one of the most important steps taken to protect the interests of the consumers. It was formulated after studying intensively the consumer protection act of a number of countries, and after through consultations with the representative of consumers, traders and industrialists. The competition act has been enacted to provide for the establishment of a commission to prevent practices having adverse effect on competition, to promote and sustain competition in market to protect the interests of consumers at large, and to ensure freedom of trade carried on by other participants in market in India, and for matters connected with or incidental thereto. With the coming into effect of the competition act, 2002 from September 1, 2009, the monopolies and restrictive trade practices (MRTP) act, 1969, was replaced and later the MRTP commission was replaced by competition commission of India (CCI). The environment (protection) act was enacted in the year 1986 with the main objective to provide the protection and improvement of environment and for matters connected therewith. The act is one of the most comprehensive legislations with pretext to protection and improvement of environment. The main objective of FEMA was to help facilitate external trade and payments in India. It was also meant to help orderly development and maintenance of foreign exchange market in India. It defines the procedures, formalities, dealings of all foreign exchange transactions in India. These transactions are mainly classified under two categories -- Current Account Transactions and Capital Account Transactions. All these acts works effectively and necessary amendments has been done time to time to maintain a healthy legislative business environment in India.

16.7 Key Words

Consumer, Consumer protection act 1986, Environmental protection act1986, FEMA act 1999, Competition act 2002

16.8 Self Assessment Test

1. Define Consumer Protection Act 1986 and its objectives?

2. What are the objectives of Competition Act 2002?

3. Define Environmental Protection Act 1986 and its importance?

4. What is Foreign Exchange Management Act 1999?

16.9 Answer To Check Your Progress

Answer of multiple choice questions:

1. a. All of the above

2. c. Both a and b

3. a. Rs. 20 lack claims

4. b. Exceeds Rs. 20 lack but is not more than Rs. 1 crore

5. c. Exceeds Rs. 1 crore

6. b. Competition act, 2002

7. a. Competition commission of India

8. b. 1986

9. d. All of the above

10. a. FEMA act, 1999

16.10 Suggested/Further Readings

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