

# Financial Foresights

*Views, Reflection and Erudition*

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**Expectations of India Inc. from  
the New Union Government**



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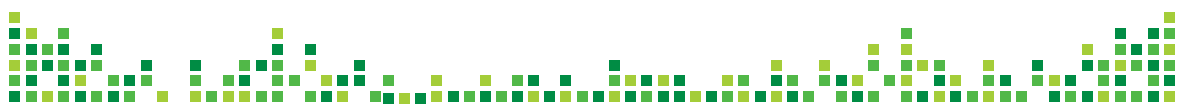
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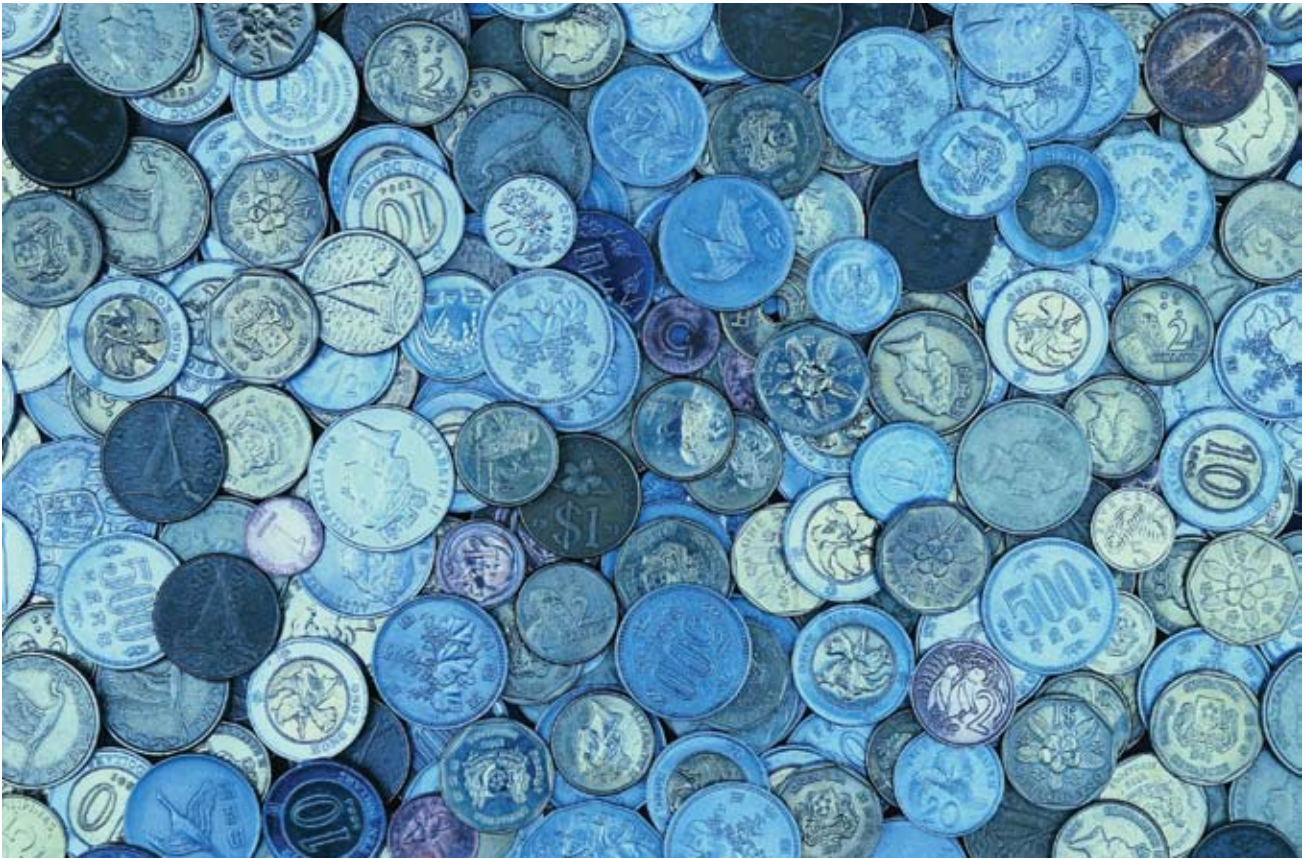
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## Expectations of India Inc. from the New Government

*Mr. Shachindra Nath  
Group Chief Executive Officer,  
Religare Enterprises Ltd.*

**F**ive years ago, there was immense flurry around India. The new buzz word around was BRIC's; where India and China were comparable and almost mentioned in the same sentence. The demographics of India within BRIC's were to be envied; a young median population, strong domestic consumption, well regulated financial sector and most of all, the world largest democracy; all the makings of a superpower growing near the 10% mark.

However, 5 years later, the ground reality is very different; GDP growth has seen a sharp decline with mentions now in the sub 5% mark, persistent inflation has the central

bank balancing the high wire between inflation and growth, litigation and retrospective imposition have not gone well with the industry; the list can be endless.

As they say hindsight is always 6/6, we should focus really on what lies ahead. This article attempts to list down a few areas which requires deliberation and immediate action by the new Government.

Governance: Coalition politics takes its toll on a nation, when different agendas fog clarity and accommodations for various polity partners have to be made. We need a transparent government which is as transparent in allocation of resources

*The participation and incentivization of the private sector is crucial to meet this demand for employment*

as is it in its functioning. These recent issues on coal, ore, spectrum and land, are true manifestations of poor governance and execution. Similarly, an austerity and end of wasteful expenditure is the need of the hour. Assets draining the exchequer year on year must be sold. Consolidation in ministries will minimize red tape.

**Tax Regime:** Both Direct (personal and corporate income tax) and indirect taxes needs to be relooked. The reality is that only 3% of the population of India show taxable income, there is a need for a wider tax net, instead of increasing taxes on those who already keep the exchequer going. On the indirect taxes front, the introduction of the GST has been put on the back burner for compulsions best known to the governance. While the roll out to have a uniform tax code by the introduction of VAT in 2005 by abolishing the sales tax started on the correct footing to establish an input tax credit mechanism to avoid double taxation. However, due to the impeded roll out and local revenue compulsions many states have increase VAT rates and blocked or reduced input tax credit ( which allowed a credit for taxes paid on intra-state purchases). This has hampered pan-India trade. We need a seamless and not a fragmented market. VAT needs to be put on the back burner by introducing a uniform tax rates, rules and laws.

**Private Sector Incentives:** Thankfully, in the last 5 years our demographics have remained healthy. Even today about 50% of our 1.3 billion people are below the age of 25. This bracket is increasing acquiring skills and higher education and to expect only the Government to meet the employment expectation is unfair. The participation and incentivization of the private sector is crucial to meet this demand for employment. Tax exemptions, grants for new job creation, weighted deductions for the



cost of new hires and their training costs are some of the incentives used globally to encourage job creation in the private sector.

According to a World Bank report India ranks 134 among 189 countries studies on the ease of starting and doing business. Currently frustrating hurdles of permissions, clearances and procedural compliance are required to start even a small legit enterprise. This has led to corruption at an unprecedented scale. Such hurdles only hurt creation of jobs, wealth and revenue earning for the government itself. Similarly, MSME's need a boost, after all they account for the largest employment after agriculture. In terms of value, MSME's account for 45% of total manufacturing output, 40% of exports and contribute to about 8% of the GDP. However, the very definition of MSME's needs a relook. Flexibility of choosing between turnover or balance sheet criterion should be allowed (employee strength being fixed)

**FDI:** FDI demand in India by some estimates is estimated to be USD 500 Billion by 2020 and could incrementally create 100 million jobs. This opportunity needs to be capitalized. All sectors should be opened with a consistent

implementation of policy, unlike the restrictive regime today where the center and states are independent to implement policy.

**Health & Education:** Our current health expenditure is barely 1% of the GDP, thus currently the burden of meeting escalating health expenses lies on the people themselves. As a result, this is the second most common reason for indebtedness of people. Though the RashtriyaSwasthyaBimaYojna is addressing the BPL populace, however, we need more cover for the entire nation. Similarly, the acute shortage of health personnel in rural areas and access to tertiary medical facilities needs to be addressed. The urban poor, drawn by employment in larger cities face the same plight and neglect.

On education our current spending between the center and the state combined is below 4% of the GDP against the global norm of 6% of the GDP by center alone. As a fallout the drop rate for students by class 10th is almost 50%. An enhance outlay and capacity enhancement with proper expenditure and execution of projects will go a long way in not only building the currently deficit skill but also lead to better jobs and a higher median pay.

All the above are expectation and only strong resolve to act on these will lift the current grid lock. Many of these stand addressed by way of bills lying on the floor of the parliament awaiting enactment. We hope that these expectations don't remain expectations but become realities.

Industry Insights Partner



**Shachindra Nath**  
Group Chief Executive Officer  
Religare Enterprises Ltd.

As the Group Chief Executive Officer of Religare Enterprises Ltd., Shachindra leads the entire integrated financial services business of the Religare Group. Religare's financial services bouquet spans across Non-Banking Finance, Retail Broking, Life Insurance, Health Insurance, Mutual Fund, Global Capital Markets, Investment Banking and Global Asset Management.

As one of the key founding team members at Religare, Shachindra has been a core pillar of Religare's successful growth journey in the last 14 years. He joined Religare in the year 2000.

Under his leadership, Religare has grown from a mono line broking led business to a diversified financial services major. Some of his marquee achievements include successfully leading the IPO process for Religare in 2007, considered to be one of the most successful IPO's in India, establishing new businesses and stitching together successful joint ventures and partnerships for the Group and raising funds through multiple private equity transactions.

Under Shachindra's guidance, Religare has transitioned into a performance orientated, bottom line focused organization and has successfully evolved from an investment phase company to a growth oriented company, ready to capture growth opportunities on a self-sustaining basis.

Shachindra is a qualified lawyer and is a University Rank holder from the Benares Hindu University. A great motivator and leader, when not at work he loves to read, contribute to columns, travel and spend time with his family.



## Expectations of India Inc. from the New Government

**Mr. Rakesh Singh**

*Chief Executive Officer, Aditya Birla Finance Ltd.*

**T**he Indian economy has had to face dual challenges over the past few years – slowing growth alongside high inflation. GDP growth has steadily decelerated from above 9% before the financial crisis of FY09 to below 5% now. Meanwhile, inflation has persisted above the central bank's comfort level of 5% since March-2008. To escape this stagflation type environment, India's government needs to implement critical structural reforms. The new government, will also need to act quickly and resolve pending issues.

Some of the key areas for reform on which the government needs to act are

**Improving the business environment:** Issues such as regulatory hurdles, rising inflation and high cost of capital have held back India's investments. The poor business environment has created an image that India is a difficult country for business and investing. India's ranking on ease of doing business as per the World Bank is 134 out of 189 countries. The recent instances of retrospective changes to tax laws have provided further credence to challenges of doing business in India. Another example is the back and forth in implementation of FDI in retail. The new government would need to provide policy

*The poor business environment has created an image that India is a difficult country for business and investing*

with long-term visibility, stability and transparency.

**Expediting project approvals:** While seeking project approvals, businesses have to deal with multiple agencies at the central and state level, which often give conflicting decisions. This is the primary reason for stalled projects and decline in new investments. The new governments needs to step in and de-clog stalled projects. The cabinet committee on investment was set up to accelerate the pace of approvals, it is necessary to continue and speed up. A single window through approach for all required clearances is desirable. These measures would go a long way in reviving capex.

**Reducing the fiscal deficit:** India's fiscal deficit has remained high over the past five years, mainly due to a slippage in revenue to GDP trends. To achieve fiscal consolidation, two options available to the government are (a) increase in tax revenues and (b) curtail spending. While weak growth in the near term would limit the increase in tax revenues, improving the quality of spending could be the first step. There is scope of reducing subsidies and bringing it line with a lower tax revenue trend. Currently, subsidies occupy around 2.5% of GDP. This poses a substantial drain on overall public savings. For example, in the case of diesel subsidies the new government should be willing to undertake a faster adjustment to make it more market linked. It would reduce the subsidy burden and relieve pressure on the fiscal deficit. A similar logic can be applied to fertiliser and food subsidies.

On the revenue side, the goods and services tax (GST) is a long pending policy reform. The system under GST would cover a wider base, reduce transaction costs, boost productivity and enable the increase in the ratio of tax-to-GDP. Though there has been some progress between the centre and states on implementation, the design has become complex and several

issues are yet to be resolved. The new government should take efforts to implement it soon.

Consolidating the fiscal deficit would help improve public saving, which would further help control the current account deficit. It would also help encourage private investments, which have sharply declined in recent years.

Improving banking capital and reducing public ownership of banks: At present corporate sector balance sheets are stretched due to high debt and high levels of impaired loans. This has adversely affected the ability of the corporate sector to make new investments. Banks' balance is also constrained while extending finance. The combination of bad and restructured loans roughly account for around 11% of the total loans of Indian banks. To help accelerate the pace of credit expansion, the government needs to re-capitalise the banking system and clean up public sector banks' balance sheets given high levels of impaired loans.

Banking credit growth was around in Apr-Feb FY14 was around 15%. This must go up to at least 20% to bring back the Indian economy on a high GDP growth path.

During cyclical downturns, bad loans' provisioning would need more capital. Given the government's current fiscal deficit targeted at around 4.1% of GDP in FY15, the ability to infuse capital into banks is limited. Government-owned banks account for at least 70% of the industry.


According to the RBI, if the government opts to maintain its shareholding at the current level, the burden of re-capitalisation is much higher. To facilitate infusion of banking capital without burdening the fiscal resources, the government's stake in public sector banks has to be brought down below 51%.

Another suggestion for raising capital is the creation of a bank holding company. It would be a special purpose vehicle, created by transferring the government stake in public sector banks. Institutional investors and private equity funds can be invited to pick up stakes in the holding company. It can raise money from the market periodically whenever the banks need equity infusion. This would help create capital and support the credit growth needed to encourage healthy economic growth.

**Providing a boost to manufacturing:** India's manufacturing growth has been stagnant or negative in the last two years. As the economy needs to generate around 12 million jobs annually to cater to the workforce, a growing manufacturing sector with increased share of GDP is essential.


There are three key areas which should be looked into:


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- Execution of the new manufacturing policy (NMP) which addresses issues such as regional disparity in industrial growth and inflexibility of labour rules. It also proposes added incentives like exemption in capital gains tax and other targets to enhance the manufacturing sector and to create additional jobs.
  - Creating new industrial corridors and improving infrastructure around access to ports and airports
  - Making land available at affordable rates for industry over the long term and making it transparent for all stakeholders
- Expediting each of the above would be critical to the success of the manufacturing sector.

Government policy can play a pivotal role in managing India's problems. A good example in recent times was the increase in the import duties on gold. This move brought down gold imports due to which India's current account deficit reached a sustainable level. A concerted effort by the government would go a long way in reviving investments and help India reach its growth potential.



**Rakesh Singh**  
Chief Executive Officer  
Aditya Birla Finance Ltd.

Mr. Rakesh Singh took over as Chief Executive Officer of Aditya Birla Finance Ltd. (ABFL) with effect from 18th July 2011. He has a total of twenty years of financial services experience with a strong track record of expertise. He has spent 18 years in the Banking industry having managed diverse businesses across SME, Retail lending, Capital Market, Mortgages and Wealth Management Products. In his last role, he acted as 'General Manager & Head - SME Banking, India', having joined Standard Chartered Bank in August 1996.

Rakesh has done his Executive Program in business management from IIM Calcutta. His academic achievements include a Master of Business Administration (Marketing) from the University of Lucknow and his post-graduation in International Relations from University of Lucknow.



## Expectations of India Inc. from the New Government

**Mr. Varoon Chandra**  
Partner, AZB & Partners, Mumbai

In light of the recent global economic crisis and the subsequent ramifications on the global economy, investors have come to be weary of investments in the Indian domestic markets. On the back of supportive global cues as well as an improving domestic economic outlook and with the expected euphoria over the formation of a new government, it is hoped that Indian markets will gain positively in 2014.

What will be key for the new government to demonstrate to market participants is that the Indian economy is open to investment and offers a stable and consistent regulatory climate, while at the same

time requiring reasonable compliance norms to ensure the stability of the markets and to provide security to all stakeholders. While the current government had introduced a number of key changes in regulations to bolster interest in market participation, some of these changes have introduced uncertainties where they did not exist before.

For instance, the recently enacted Companies Act, 2013, has introduced ambiguity on a number of issues after the Government of India has notified a vast majority of the sections of the new legislation. While a few key provisions continue to be governed by the 1956 Act, it will be critical over the

*The recently enacted Companies Act, 2013, has introduced ambiguity on a number of issues after the Government of India has notified a vast majority of the sections of the new legislation*

coming months and with the change in government to examine how the new provisions will interplay with what regulators have been trying to achieve. For instance, regulators have been trying to bolster the domestic bond market and encourage public issues of bonds coupled with increased retail participation in the bond market. However, certain provisions of the Companies Act, 2013 are not conducive to encouraging increased bond issuances and participation. For example, under the rules which have been enacted with respect to Section 71 (3) of the Companies Act, if a company issues secured debentures, the debentures must be secured with “specific” property of the company. A charge on specific property would seem to imply that a floating charge over “non-specified” current assets does not qualify for the purpose of securing debentures. In case of several bond issuers such as NBFCs, there are no assets other than current assets to secure the debentures, which would render it difficult for NBFCs to issue secured debentures. Further, with respect to privately-placed bonds which are listed by private limited companies, under the 2013 Act a private limited company listing its bonds, it becomes a “listed company” under the 2013 Act, thereby invoking several more onerous corporate governance norms. While the Securities and Exchange Board of India (“SEBI”) had ensured that under the debt listing agreement there was not too heavy a burden on private companies listing their debt securities, this distinction has not been taken care of in definition of “listed companies” under the 2013 Act. Therefore private companies may be discouraged in listing privately placed bonds.

Further, while put and call options have existed in private arrangements between shareholders (particularly in the context of private equity investors), the enforceability of such options has always been a matter of debate. In an environment where exits for such



investors are heavily dependent on cooperation from the Indian promoter, this uncertainty was discouraging for investors. In order to address this uncertainty, SEBI had permitted persons to enter into contracts for sale or purchase of securities containing (i) pre-emption rights (including right of first refusal rights, tag-along or drag-along rights); and (ii) options for the sale or purchase of securities (where the title to the securities is held by the selling party for at least one year from the date of the contract and the contract is settled by way of actual delivery of the underlying securities). However, there are still a few issues that need to be considered with respect to put options, for example, whether a put option in the articles of association of a company undertaking an IPO would be permitted to continue subsequent to the completion of the IPO. Further, SEBI has taken steps to remove some of the uncertainties around “put” / “call” options on securities of public limited companies, the Reserve Bank of India (“RBI”) released a circular dated January 9, 2014 stating that such options / rights may be exercised by foreign investors, as long as such options do not provide the foreign investor assured returns, subject to the following: (i) in case of a listed company, at a price not more than

the prevailing market price; and (ii) in case of unlisted companies, at a price not exceeding that arrived on the basis of Return on Equity (“RoE”) as per the latest audited balance sheet. RoE has been defined to mean profit after tax divided by the net worth, and net worth includes free reserves and paid up capital. This development again is likely to have a negative impact on foreign investors. An RoE valuation is an indicator of the financial performance of a company during a specified period, and may not convey the actual fair value of the securities of the company. Further, it is not clear whether the intention of the RBI is that the RoE valuation should be applicable even in the case of a put option triggered by an event of default by the resident, and additional clarity is awaited on this.

It is further expected that in order to encourage foreign investors, the new government may seek to modify the policy on foreign direct investment, permitting restricted sectors in which foreign investors are interested, including inter alia sectors like insurance, education, and infrastructure. Increasing the sectoral caps and allowing more foreign direct investment in these sectors may result in India being viewed as a more ‘open’ economy and result in higher



foreign equity participation in these traditionally closed sectors.

A new government will also influence a change in thinking from the perspective of regulators. Perhaps one of the ways in which this could be achieved could be for the Government to work with regulators and ensure that while norms set by the regulators are met, the regulators ensure that the regulatory framework does not significantly impede growth. For instance, while the RBI had come out with a promising set of Guidelines for Licensing of New Banks in the Private Sector in February of 2013,

and had opened applications for awarding banking licenses for the first time in a decade, ultimately the RBI chose to be conservative in approach and award licenses to only two applicants. While the RBI in its press-release dated April 2, 2014, stated that it intends to issue licenses more regularly, the new government could play an active part in ensuring that applicants which meet governance norms set by the RBI are issued banking licenses expeditiously to further develop the banking system and enhance the reach of the banking network across the country.

The aforementioned examples are certainly not exhaustive of our expectations from the new government and are not the only changes we hope that the new government brings about. In addition to the examples set out above, the new government will need to take active measures to ensure that any initial euphoria post the elections does not exhaust itself and that India is projected to investors as an economy that is open to business, that has a regulatory friendly investment climate juxtaposed with stable and secure markets, and that is poised for further growth and expansion.



**Varoon Chandra**  
Partner  
AZB & Partners, Mumbai

Varoon Chandra is a partner at AZB & Partners, Mumbai. He graduated with a Bachelor of Laws degree from the National Academy of Legal Studies and Research, Hyderabad in 2004. He is registered as an advocate with the Bar Council of Maharashtra & Goa.

He has been with AZB & Partners since 2004 and was designated as a partner in 2011. Varoon's key practice areas have been capital markets, securities law and cross-border mergers and acquisitions. As a part of the securities law team, he has been involved in a number of international and domestic capital market transactions, including issuance of foreign currency convertible bonds and global depository receipts as well as Indian initial public offers, rights issues and qualified institutions placements. He has drafted and reviewed offering documents, conducted due diligence and advised issuer companies as well as underwriters on Indian law issues.

In addition, he has also advised on securities regulations issued by the Securities and Exchange Board of India pertaining to matters such as takeover regulations, the investment/acquisition of shares in Indian listed companies, insider trading in the context of investment/ acquisition of shares in Indian listed companies and the listing of companies on Indian stock exchanges.



## Expectations of India Inc. from the New Government

*Mr. Sandeep Ghosh , Managing Director & Chief Executive Officer, &  
Mr. Rahul Baijal , Fund Manager,  
Bharti AXA Life Insurance*

Probably the biggest set of expectations from the new government would be in the area of improving governance at various levels. Over the recent years, the industry has suffered a lot due to the so called “policy logjam”. There is clearly a strong need for the new Union government to improve inter-ministerial coordination and bureaucratic administration which has been below the mark in recent years. Also there has to be greater consistency in policy making. Unfortunately, due to the various scams in the recent years as well as some announcements on retrospective amendments to tax laws has all led to perception of inconsistency. It is

very important for government policies to be consistent and predictable. This will improve business confidence and allow businesses to plan long-term and enhance India’s reputation as an investment destination. There is also a need for the PMO and the central government to improve Centre-State relations and bring different opinions to the table and achieve more effective political consensus on key legislations. The morale in the bureaucracy needs to be boosted too. The various corruption scandals has made the bureaucracy risk averse and the PMO has to re-instill confidence in it and give political support to accelerate decision making and effective ad-

*It is very important for government policies to be consistent and predictable. This will improve business confidence and allow businesses to plan long-term and enhance India’s reputation as an investment destination*

ministration. Addressal of the issues mentioned above will allow for faster decision making and implementation on the ground and accelerate the process of economic revival.

### Some recommendations across sectors:

**Sustained fiscal consolidation to provide headroom to cut interest rates:** One of the first tasks of the new government in our view is to stick to the medium-term fiscal consolidation path and provide a good budget which is indicative of the same. Persistent high fiscal deficit post the financial crisis has resulted in high inflation which has kept interest rates elevated. Some good steps have been taken by the current government on this front over the last many quarters (e.g. diesel price deregulation) but a lot more needs to be done. Not only does the new government need to continue to cut fiscal deficit, it has to improve its quality by reducing revenue deficit and stepping up capex. This will augment domestic capacity creation and actually help reduce inflation and create headroom for RBI to start cutting interest rates and provide a monetary stimulus to the economy.

**The issue of clearances** – Re-instilling a sense of confidence in the private entrepreneurs who have suffered a lot due to bureaucratic/procedural delays is very critical to make them start spending again on new business plans. They need to get back the comfort that clearances and approvals would be obtained or denied in a time bound manner so that entrepreneurial energy is focused on managing the real business rather than managing the environment.

**Long-term vision in certain sectors** - The government can do a much better job in showing better long-term vision in certain sectors like defense and electronics manufacturing where India is a large importer as domestic manufacturing has not been encouraged. This has hurt India's external balance

and thus the currency. India needs a credible long-term policy to encourage domestic investments in these and lead to import substitution besides creating and other sectors which can generate jobs, help improve external balance and also reduce scope for graft (in defense).

### Measures for reviving the investment cycle

Lack of timely and appropriate decision making by the government or what has often been described as "policy paralysis" has to take a large part of the blame for slowing the investment cycle. In context of the generic recommendations, there are specific steps that the government could take to revive investments in the infrastructure sectors.

**Power sector.** We need to improve the coal availability in India and reduce dependence on imported coal. India has abundant coal reserves but not utilized properly. Coal production volume has slowed sharply for both Coal India and the private coal miners. We need to restart the process of greater private sector involvement /PPP models. Greater clarity will emerge post the investigations and ongoing litigation on the coal block auctions. The new government should work towards quick closure on the same and move on to the next level of formalizing a new policy on coal blocks. Creation of a coal regulator could be a wise step in this direction to accelerate the process.

**Roads & transportation:** About 8,000kms of highways have been awarded for almost two years now but work in progress has been quite slow on most of these projects. The concession document under the PPP models clearly enunciates strict timelines which have been breached in many cases. Some have been wrongly/aggressively bid/some faced bottlenecks in execution- land & environment approvals /lack of financial closure. Various other transportation

projects (metros, railways, ports) are on the drawing board for a number of years. Devising a strict timeline to take a decision whether the projects are feasible or not/weed out the infeasible ones and expedite work on the ones found feasible are some of the early steps the new government can take. A possible solution for the aggressively bid projects in the roads sector is to either cancel all such existing contracts and ask for fresh bids or maybe a rule based relief package for the entire industry which is somewhat revenue neutral to the government.

### Key legislations which can be focus of the new government

**Goods and Services Tax (GST):** A move forward to closure on this bill would be a big boost to the economy. GST aims at simplifying India's indirect tax structure and make India into a single pan India market. This will give a significant boost to productivity and logistics industry. Estimates suggest that this measure alone could boost India's GDP by 2-3%. The GST is however stuck due to differences between the centre and the state governments. The differences as we understand are largely procedural in nature and the central government needs to give some concessions and flexibility to state governments (which otherwise lose their revenue flexibility).

### Insurance Bill

The long-awaited insurance Bill has been pending in the Parliament for many years. Foreign insurers have patiently awaited the outcome of our democratic process of building political consensus. Time is now running out. There seems to be a growing apprehension among them of a political impasse continuing in 2014 and beyond. India needs long-term foreign and domestic capital to invest in our insurance industry. It is critical to protect human life, our productive assets and be a key resource for the country's

infrastructure. Moreover, the FDI cap of 26% in India is amongst the lowest in the world. In Asia too – most other countries like China, Malaysia, and Philippines have higher limits. Some countries like South Korea and Taiwan even allow 100%. We think it is time for increasing the FDI cap to 49%. If we do

not seize the opportunity to encourage more capital, our long-term growth will be derailed. Besides job creation in a human intensive industry - FDI inflows would also help contain the current account deficit and keep the currency stable in an uncertain environment for emerging market currencies.

**Direct taxes code:** Direct taxes code aims at simplifying India's direct structure. While not as dramatic as the GST, this legislation too will have an impact on tax compliance and thus tax buoyancy. It will also lead to more predictability and thus lower disputes which too is a long-term positive.



**Sandeep Ghosh**  
Managing Director &  
Chief Executive Officer  
Bharti AXA Life Insurance

Sandeep Ghosh is the Managing Director & Chief Executive Officer at Bharti AXA Life Insurance since May 2011.

He has over 20 years of experience in India and overseas, primarily in the financial services sector. Prior to joining Bharti AXA Life, he was with ANZ as the Managing Director, Commercial Banking Head for Asia Pacific based in Hong Kong. During this time, he played a major role in building a commercial banking franchise for ANZ in Asia through organic builds and the integration of businesses acquired from RBS.

Before joining ANZ, Sandeep spearheaded the Commercial Banking for Royal Bank of Scotland in Asia. He was responsible for Business Banking, SME & Middle Market client franchises, managing a team of over 1,000 bankers and 40,000 client relationships across 9 countries.

Prior to this, he was with Citibank for 9 years during which he held various roles, lastly as Managing Director for the Global Commercial Bank in India. During his tenure, he led the India business to become the largest organically built commercial banking franchise within Citi.

Sandeep has also worked with PepsiCo in the Marketing function as the Category Marketing Director for Flavours and Alternate Beverages for the South Asia Business Unit. Sandeep began his career in 1990 with Coats Viyella PLC in the UK. Over a span of 5 years, he worked in a variety of Marketing and Business Development assignments across Europe, the Middle East & North Africa.

Sandeep holds a Masters in Business Administration (PGDBM) from Indian Institute of Management, Ahmedabad and has a Bachelors degree in Accountancy & Financial Management from Sydenham College, Mumbai University.

Rahul Baijal is a Fund Manager in the Investment team at Bharti AXA Life Insurance since June 2012.



**Rahul Baijal**  
Fund Manager  
Bharti AXA Life Insurance

He is a Finance professional with more than 15 years of work experience primarily in the field of Equity Research and Fund Management. Prior to joining Bharti AXA Life he was a Fund Manager/Director at Voyager Capital, an India dedicated equities fund with financial institutional investors and family offices across US as the primary investor base. During this period he played a major role in helping the company and the fund scale up from a start-up to peak assets under management of >\$US 350mn. Before joining the fund management side, Rahul spent five years as an equity research analyst at Credit Suisse and HSBC securities covering the consumer and the pharmaceutical sectors. He was part of the Asiamoney and Institutional Investor ranked teams in his stint over there.

Rahul holds a Masters in Business Administration (PGDM) from Indian Institute of Management, Kolkata and a B.E. in Electronics & Communication from Delhi College of Engineering, University of Delhi.



## Move at a Breakneck Speed

**Mr. Rashesh Shah**

*Chairman, FICCI's Maharashtra State Council &  
Co-Founder & Chairman, Edelweiss Financial Services Ltd &  
Managing Director, ECL Finance Ltd.*

**T**here are a couple of things playing top of my mind that any government coming to power will have to tackle. These include the prickly issues of inflation, infrastructure and job creation. I want to deal with these because I think all of them interlinked.

Allow me to deal with inflation first. There is a school of thought that argues it is a necessary condition, which accompanies growth. Implicit in this statement is the argument that high growth is inevitably accompanied by high demand. Market forces then come into play and inflation becomes inevitable. To that extent, this school of thought argues, if we desire GDP growth rates in the region of 8-9

percent, then we might as well learn to accept inflation at the levels it is in right now. Simply put, if there is more money chasing goods, it is but natural that the prices of these goods will go up.

I come from a school of thought, which believes this need not be the case. Instead, look at it from a perspective that if there are enough goods in the system to meet the demand money places, prices of goods will stay low. This is important because India is a country where large masses of the population don't have the wherewithal to handle an inflationary economy—even if you provide them high growth and the so-called benefits that accrue from it.

*Investments in infrastructure development to create linked pathways between all the different Tiers; building of roads, bridges and homes while easing communication & transportation will help migration between different urban and semi-urban centers*

A clear indication is the fact that high inflation is usually a pointer that available productive resources are not being put to the best use. To use but just one indicator, the passenger vehicle industry currently has a capacity utilization in the region of just 50 percent.

When extrapolated into a larger context, this number does explain some of the dilemmas Indian industry faces – weak balance sheets, underleveraged assets, and subsequently low productivity.

Going one step further, I'd argue, these are the kind of variables that can have an adverse impact on long-term social stability as well. I sincerely hope, therefore, policy makers in the dispensation that comes into power next, burn the candle at both ends and work overtime to keep this number under check.

In doing that, they will inevitably set their sights on creating the right environment for development of infrastructure, manufacturing and services businesses, and finally job creation, which is what India needs most right now. Needless to add, we don't have too much time on hand to do that either.

### The demands of the young

By 2020, the median age will be 29, making India the youngest nation in the world. The kinds of demands a young population can place on policy makers are enormous. Unlike the more patient and older predecessors, the young will be impatient and demand better opportunities to further their interests. The demands they place are fair and it is incumbent on the government that comes to power to help this generation realise and unleash their potential.

It is important to note that in spite of the kind of pressures and battering the economy has been subject to, FDI inflows were up 17 percent to USD 28 billion last year. Initial forecasts for this year and the next indicate the number will only grow. As much as this is a



good sign, there are times I think of FDI a fickle number. It doesn't take this money too much to find its way into other parts of the global economy where the macroeconomic variables sound more stable and promising.

This brings me back to the earlier point on the need to focus around infrastructure, manufacturing and services.

In large part due to the changing demographic I've articulated above, the pressure to urbanize will be high. It has been demonstrated time and again, a younger population would much rather live in an urban conglomeration. As they make the shift to the traditional urban centers, pressure on infrastructure here will mount. So while on the one hand, the government will have to build robust infrastructure, it will also have to develop Tier II towns into more habitable dwellings. Investments in infrastructure development to create linked pathways between all the different Tiers; building of roads, bridges and homes while easing communication & transportation will help migration between different urban and semi-urban centers and open up avenues for people to seek better jobs and lifestyles.

Linked very closely to this urbanization will be the move from an agrarian economy into a manufacturing and services led state. The proclivities

of a demographic that lies at a median of 29 will lie in some part towards manufacturing and in very significant numbers towards services.

In the medium term, the needs of a good part of this population can be taken care of by better capacity utilization in the manufacturing sectors. As mentioned earlier, there is a lot of under utilized capacity here that needs to be deployed so jobs can be generated. A simple idea like promoting those who had booked their tickets well in advance to the empty first class and then accommodate as many of those on the waiting list in the second class, brought down railway's losses by a huge margin. This goes to prove that there is no dearth of geniuses in the government machinery. All that is missing is a strong political will. If I were to project myself a little further into the future, though, I am willing to bet this demographic will have to move towards services and entrepreneurship and the government in charge will need very clear policies in place to manage this transition.

It seems inevitable that, much like agriculture, manufacturing will move towards automation as it has in developed economies. This leaves only the services sector to generate employment. Here too, the pace at which globalization is happening may seem threatening from an Indian perspective. While

India was the backroom to the world in the late nineties and the first decade of this century, other South Asian and emerging African economies are quietly stepping in and claiming the same status today.

Any government that comes to power will do well to stare this changing dynamic in the eye and start work earnestly at recycling and putting in place an entrepreneurial friendly economy. The newborn South Africa under Nelson Mandela is a clear example. The government made minor changes in the procurement policy, mandating that 20% of the

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goods be purchased from companies promoted by economically and socially weaker blacks. This not only energized an indolent manufacturing sector but also brought about enormous social justice without any heartburns. In India, if that means

easing tax burden, cutting red tape, organizing the generally disorganized MSME sector and removing every obstacle that can possibly come in the way of entrepreneurship, then it had better be done ruthlessly and at breakneck speed.



**Rashesh Shah**  
 Chairman, FICCI's  
 Maharashtra State Council &  
 Co-Founder & Chairman  
 Edelweiss Financial Services Ltd &  
 Managing Director  
 ECL Finance Ltd.

Rashesh Shah is the co-founder and Chairman of Edelweiss Financial Services Ltd and is the Managing Director of ECL Finance Ltd.

He has over 25 years in financial markets and the corporate sector. He founded Edelweiss in 1995 and has since grown the Edelweiss Group to become a diversified financial services organization with businesses ranging from Credit (Wholesale, SME, retail finance and housing finance), Financial markets, Insurance and Commodities.

Rashesh serves on the Boards of various companies and public institutions serving as Chairman, Maharashtra Council of FICCI as well as on the SEBI (Stock Exchange Board of India) committee to review Insider Trading Regulations.

Among the several accolades Rashesh has received, are the 'Entrepreneur of the Year' award from Bombay Management Association (2008-2009) and the 'Special Award for Contribution to Development of Capital Markets in India' by Zee Business 2011. Under his leadership, Edelweiss has received numerous awards, the most recent being 'The Best Managed Mid Cap Company in India' by Finance Asia, Hong Kong and 'Best Corporate Governance, India' by Capital Finance International, London, UK.

Rashesh's academic qualifications include an MBA from Indian Institute of Management, Ahmedabad, a Diploma in International Trade from the Indian Institute of Foreign Trade, New Delhi and a Bachelor's Degree in Science from the University of Mumbai.



## Expectations of India Inc. from the New Government

*Dr. Naresh Maheshwari*

*Chairman, Farsight Group & Chairman, DPAI*

Outcome of general elections 2014 which created unprecedented hype and media attention globally is expected shortly. Not only the masses but also the corporates have euphoria of hopes and expectations from the new government.

India was saddled with problems of stagflation, policy inertia resulting in low capacity utilization and low productivity. Global melt down added woes to the Indian economy and a sharp volatility and depreciation was observed in Indian currency, foreign trade, balance of payment, etc.

The people expect the new Government to be transparent, corruption-free and development

oriented. Therefore, it would become fulcrum to attract investment including FDI. It has no option but to take expeditious actions on precarious state of economy where, on one hand, large numbers of projects are lying stalled and on the other hand there are shortage of electricity, coal, raw material, etc. for our industry. This has increased our dependency on import alarmingly.

We must understand limitations of the present government. Even if the NDA comes with majority they will remain in minority in RajyaSabha till at least next election of RajyaSabha, which practically means almost two years. It implies that action has to be done within the existing legislative

*If the economy has to be restored, back on the track of growth, issues of unemployment and inflation are to be tackled*



framework. Fear of poor monsoon may fuel inflation and will be an obstacle even if RBI wants to lower the interest rates. Similarly ever going deficit will afford hardly any avenues in providing relief in taxation. As a matter of fact, citizens have to be ready for increased costs in terms of reduction or rationalization of subsidies or imposition of additional tax on luxuries. But the deep consolation, solace and satisfaction would be Transparent, Accountable and Decisive Government. Discussing policies and solutions may not be enough unless these are discussed thoroughly and are implemented diligently. It will be the burdened duty of new government to ensure that Parliament functions and sessions are not washed out.

If the economy has to be restored, back on the track of growth, issues of unemployment and inflation are to be tackled; the following key issues are to be addressed immediately and are the legitimate expectations of India Inc. from new Union Government.

### Revival of Manufacturing Sector

India's manufacturing sector is shrinking and the Government needs a roadmap to revive this very crucial sector of the economy. It is not feasible to expect Indian manufacturing companies to compete with the rest of the world with their hands tied. India's share of global manufacturing stands at little over 2 percent.

The government is expected to adopt a multi-pronged approach revolutionizing regulatory regime in manufacturing sector by expediting approvals, and reviewing regulations related to land acquisition, mining, environmental clearance and documentation. There are large number of Industrial Acts which can be re-codified and unified into a single Code which will eliminate multiple and often contradictory definitions. For example, "factory", "wages" have been defined in different Acts

in different manner. No doubt the law has to meet the legitimate expectations of working force but it should not create bottlenecks for the industry. Present industry is manned by highly skilled and educated work force as most of the jobs pertaining to unskilled labor has been mechanized and automated. This class has different aspirations and requires different types of protections. Therefore it is expected that the Industrial law will be realigned and re-written giving full focus on computerized compliance, clarity, protection coupled with accountability.

Government may come out with a moratorium for two years for compliance of technical issues and outdated laws, pending codification as suggested above.

### Decentralization of more powers to State

The large number of matters which are impeding the economic growth falls in the concurrent list and there is no policy framework available. Article 254 of the Constitution provides that central government can delegate powers to the State to make the requisite laws. If these matters are delegated to the states, then the states will be able to make their own legislations and present state of total inertia will be evaporated. Thus if any state wants to go aggressive in any development model, they should be allowed to do so, instead of waiting for a central legislation which is difficult to pass keeping in view the multiple polar politics between central and state governments. Some of the illustrative items which central government can give to state are education, agricultural marketing, industrial dispute, warehousing, labour, warehousing and health.

This model can be further advanced if allocation to states is made from centre on the basis of achievement of mutual accepted outcomes.

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### Accelerating SME (Small and Medium Enterprises) Sector

SMEs are widely distributed across the country and producing a diverse range of products to meet not only the needs of the local markets, but also of the global market. Cottage and traditional sector have always been a foreign exchange earner. Of late, SME has seen a sharp decline because of various reasons such as non-availability of skilled labor, relocation of industry because of various environmental laws, high interest rates, etc. Cheap and unrestricted import from neighboring countries is also affecting local entrepreneurship. In some cases it has been observed that industry has put up manufacturing units in the neighboring countries to take benefit of local conditions such as cheap labor, cheap electricity and non-interference from inspector-raaz and from there

manufactured goods are being imported into India. This has resulted in flight of scarce Indian capital and is adding to the Indian import bill. On other hand, it is contributing in growth and development of other countries and creating a competing super-economic power. New government has to make a roadmap as how they can compete with the benefits offered by the neighboring countries resulting into production of goods at lower cost.

The government needs to strengthen the SME sector units through promotion of quality competitiveness and research and development. Presently, even a SSI has to comply more than 35 Factories Act and Industrial law which are major hurdles in development of SME sector. These again have to be re-codified to avoid delays and bureaucratic interference. Most of the provisions of the Act are applicable if numbers of employees are more than ten/twenty. This should be increased minimum to fifty, keeping in view the change in level of education, skills and bargaining power of work force.

SME are suffering because of multiple taxation resulting into multiple compliance. SME having turnover below a prescribed limit say 200 lacs should be subjected to a single tax based on turnover which should take care of income, sales tax, VAT, excise, etc. this single tax can be apportioned between state and central governments. But the SME sector would be required to file a single tax return. It is expected that the new government will engage in some out-of-box thinking and will come out with radical plans to revitalize the SME sector.

### **Rationalization of Taxation**

UPA government introduced DTC (Direct Tax Code) promising panacea and solutions to all vexed issues of taxation. Government is looking for increased revenue to meet out its commitment and fund its all galloping



expenditure including subsidy, interest and defence outlays. Therefore, it is essential to plug loopholes, increase coverage and find out new avenues in any taxation policy. But any overdose of taxation is counter-productive. It increases incentive for evasion and leaves fewer amounts for household and industry development. More than the rate of tax non-clarity about many exemptions and applications of provisions irritates the honest taxpayers.

#### **Increase in basic exemption**

Basic exemption limit be increased to Rs. 3.5 lacs. Aggregate amount for deductions in savings be increased to Rs. 1.5 lacs. Therefore, upto income of Rs. 5 lacs should be tax free. Beyond that rate should be reasonable as provided in the new DTC. A large number of exemptions and deductions be unified and re-codified.

#### **Rationale for Transaction Tax**

World over economists are of the same opinion that any tax on transactions distort the market equilibrium and price discovery mechanism and therefore, should be avoided. More so in a developing economy where markets are imperfect, unorganized and major turnover occurs outside the official market. Therefore, any tax on transactions be it mandi tax, APMC tax, securities

transaction tax (STT) or commodity transaction tax (CTT), be avoided.

#### **STT (Securities Transaction Tax) v/s Long term Capital Gains exemption**

The concept of exemption of long term capital gains itself require a re-examination. STT and Long term capital gains exemption cannot be traded off. Moreover, it is feared that long term capital gain exemption has benefitted only promoters or the large financial institutions at the cost of small and marginal players who hardly made any gains but kept on paying STT.

#### **Should Dividends be taxed?**

DDT was introduced as it was difficult to tax dividend in the hands of millions of investors, cost of administration was high, there was TDS on dividend beyond a limit and reconciliation was also a problem. Further there was double taxation of dividend in case of corporate shareholder.

However, there are unintended consequences of DDT wherein a small investor is subsidizing a big investor. DDT seems government's contribution to promoters since the tax is paid by companies as the dividend comes tax-free to promoters.

Further, insertion of Rule 8D ("Method for determining amount of

expenditure in relation to income not includible in total income”)in Section 14A of Income Tax which provides for, provides for disallowance of not only direct expenditure incurred for earning the exempt income but also for disallowance of proportionate indirect expenditure & that of 0.5% of the average value of investment.

This is causing lot of litigation as well as unfair treatment to an investor as the tax paid by company on its income and dividend distribution tax goes from the pocket of investors only, thus, putting another disallowance and that at the rate of 0.5% of the average investment value leads to 3 times taxation on the same income.

It is, therefore, suggested that the section should be suitably amended or CBDT should clarify that S. 14A should not be invoked where income is received by the assessee after payment of tax under the Income-tax Act.

Scope for Voluntary Disclosure:

Any voluntary disclosure scheme attracts different opinions. It goes against the honest taxpayers, yet keeping in view the vast amount of black money generated in the last decade, there seems to be no other option. Any scheme in this direction has to be carefully drafted where it does not seem giving incentives to the dishonest tax payers. Money should be collected separately and be utilized in specialized projects.

Government should come out with an effective policy which can unearth black- money and further generation of black money can be eliminated. In the past, many schemes with different models were floated. However, government may come out with a scheme similar to the Special Bearer Bonds scheme where collected funds can be invested in mega infrastructural projects.

#### Pro- active Tax Provisions

To attract foreign investors, it is of the essence for the new leadership to focus on renegotiate certain tax treaties, stabilization of tax policies, doing away with retrospective taxation.

If tax measures advocated by the industry bodies are endorsed by the government such as introduction of GST, reducing the corporate tax rate to 20% and apply it on consolidated GAAP profits from Indian operations, tax dividend income and capital gains at marginal tax rate, it will go a long way in augmenting growth in industrial output and increased investment by the foreign players.

### Foreign Investments

We recognize that India is a capital scarce economy which needs FDI in key sectors viz, multi- brand retail, defence, and banking. To see the importance of FDI in a promising economy, India needs only to look to rival China, where foreign manufacturers have helped to create huge economies of scale and transferred – sometimes unwillingly – enormous expertise.

Of late there has been bout of reform and liberalisation measures done to revive investors’ confidence and flow of foreign funds to India Inc, t here is still room for a lot more.

For instance, government can move to a regime of free pricing for transfer of shares between resident and non-resident i.e. the buyer and seller should be free to decide the transaction price. Then, there shouldn’t be any need to obtain approval from the RBI in

cases where deferred consideration is received from foreign acquirer of shares of Indian company.

Most importantly, giving national treatment to foreign owned companies, and more importantly a stable policy regime is essential to attract continuous flows of investments.

### E-Governance

E-Governance, endowed with transparency, expediency and accountability, can be a lethal weapon to rule out biggest problem of the country, i.e. corruption. Many studies suggest that electronic delivery of services (e.g., submitting internet applications and tax returns for computer processing) can reduce corruption by reducing interactions with officials, speeding up decisions, and reducing human errors. E-government can lead to centralizes data which can be used for improving audit and analysis.

As taxpayers are important partners in generating revenues for national endeavors, the honest taxpayers should be awarded in recognition of having met national responsibility. They can be provided a tax-compliance certificate to a firm to help it build an image; and requiring tax certificates to renew some types of licenses.

All the three limbs of government:



Legislature, executive and judiciary need to kick start the code of conduct and the watch dog agencies. With the huge groundswell of public anger, civil societies and social movements have already come to life, more active and responsible participation of the government is anticipated. Accountability and transparency must be generated by the combination of

political will from the top and public pressure at the base.

### **Conclusion**

Although, path of the new government is very difficult due to accumulated budgetary deficit, poor expected monsoon, not having majority in Rajya Sabha. Yet we expect the government to make a paradigm

shift in reviving growth, bringing stable and predictable policies and more important the transparency, accountability and sensitivity. These factors alone will bring confidence to the people and all other stakeholders which are catalyst to the growth of the country. Expectations of India Inc. may not be fulfilled overnight but well begun would be half- done.



**Dr. Naresh Maheshwari**  
Chairman, Farsight Group &  
Chairman, DPAI

Dr Naresh Maheshwari, FCA, FCS, FISA, doctorate in options trading, is Chairman of Farsight Group, a well known broking house of India He is a prolific commentator on matters pertaining to Capital Market, Investors Protection and Corporate Laws in electronic and print media.

Dr. Maheshwari has been associated with many trade bodies. Founder and Past President of Commodity Participants Association of India (CPAI) and Past President of Association of National Exchanges Members of India (ANMI). Former chairman of ASIA forum for Investor Education (AFIE) , South Korea, Comprising of 31 organization of 21 counties having vibrant Capital Market, he is now member of SEBI Secondary Market Advisory Committee.

He has visited and represented Indian capital market in many international organizations like KOFIA Korea, ASC Thailand, MAS Singapore, various stock exchanges at Hong Kong, Shanghai (China), Korea, Bursa Malaysia, SMX etc. Dr Maheshwari also led Indian capital market delegation to Asian Securities Forum at Beijing and Tokyo. He was observer in ICSA (International Council of Secretary Association) AGM-2011 at London and ICMA (International Capital Market Association) AGM-2011 at Paris.

A hand book for Investing & Investor Protection authored by Dr. Maheshwari published by Institute of Chartered Accountants of India was released by Mr D. K Mittal, secretary Ministry of Corporate Affairs Govt. of India.



## Expectations of India Inc. from the New Government

**Mr. Sandeep Bakhshi**  
MD & CEO,

*ICICI Prudential Life Insurance Company Ltd.*

India, the largest democracy in the world, has come a long way since the opening up of the economy in 1991. We have secured a significant position in world economy and are considered to be the world's third largest economy in terms of Purchasing Power Parity as per the World Bank's International Comparison data.

If we take a closer look, we would see that there is yet a lot more that we are capable of achieving given the demographic advantage – the fact that by 2020 a big portion of our population will comprise of young-working individuals. The strong presence of an ed-

ucated and financially aware working-class, supported with relevant reforms will make India one of the preferred destinations for international investors and provide the required fillip for our need for capital to transition from an emerging economy to a developed economy.

The Indian life insurance industry has witnessed changes at periodic intervals which started with the opening of the sector for private players in 2000. The regulations have been formulated by factoring in the changing the needs of the customer, the macro-economic environment and envisaging the long-

***The ability to secure more and more lives by leveraging the available technological solutions can place India ahead of other countries – considering the vast untapped potential***

term impact this would have on the financial security and independence of the country's population.

We have been able to come this far thanks to the support of the Regulator whose key focus has been that of protecting customer interests. The increasing competition has been an enabler of sorts, pushing the industry players to maximize their potential and harness in-house expertise thereby offering greater number of options and more convenience to customers.

Innovation has played a big role in the industry and impacted products and distribution encouraging insurers to constantly keep raising the bar and creating new benchmarks. While a multi-channel distribution approach has made it possible for insurers to overcome geographical boundaries, growing technological support has facilitated on-the-spot transparent sales and issuance of policies powered by real-time underwriting and e-KYC. Another milestone has been that of dematerialization of policies. All these changes have had a positive impact and above all has changed the way consumers look at life insurance.

Reforms are drivers of growth as they help to make the products and services much more relevant. With the passage of time life insurance products have become more customer-friendly – the charge structures have been rationalized and are comparable with other financial services products. The unique ability of life insurance to provide protection and an avenue to build savings necessitates them to be an integral part of an individual's financial portfolio or plan.

Given the fact that a big portion of our population is still untouched by life insurance certain reforms on the product and distribution front can be considered.

On the products front, a simpler and a standardised product combined with a seamless process can further enhance the on-boarding experience for customers. The approach for new product

introductions could involve a 'use and file' system for a set of standard products. These standard products could be based on principles of protecting customer interest and ensuring value delivery. Such a system would mean a 'management by exception' approach where the insurers certify adherence to the standard product principles. For any new category or product structure, the existing file and use system could be followed. In such a scenario a product structure approved for any insurer could be made available to all insurers. This approach could simplify the products, fast track the product approval process and also help the insurers in leveraging technology.

A simple one-page policy application form could be considered for all standard products. This would further simplify the customer on-boarding process, make it more transparent as well as efficient. The benefits of technology are manifold, dematerialization of policies could be taken a step further to facilitate an integrated KYC process across the financial services sector – which would be an enhancement to the existing e-KYC process. The multi-channel distribution architecture too could be reviewed with reference to the compensation structures – creating structures that would be more channel-specific thereby encouraging distributors to leverage their ca-

pabilities in the best possible manner.

A significant part of our population employed in the organized and unorganized sectors as well as those who are self-employed do not have any provision for regular income after retirement. Flexibility in allowing insurers to provide liquidity options as well as returns would enhance interest in pension products and expand the overall market for life insurance companies. Other facets too which can be considered are the availability of suitable instruments enabling the development of long term products while providing relevant options for hedging risks over the long term. Allowing fixed term annuities could lead to renewed interest among the life insurers to manufacture relevant products. Another initiative could be to that of allowing the employees to choose a pension plan for accumulating contributions to their EPF. The introduction of post-retirement health products would provide a protection cover when it is required the most. Tax incentives made available for such investments would further increase their uptake.

Financial inclusion forms an important part of the life insurance business. Securing the lives of the population in rural India is an imperative. The emergence of Common Service Centres and the draft guidelines for micro-insurance are formative steps towards the



betterment of the economically challenged sections of society.

The future holds a lot of promise for this emerging sector. An increase in the savings ability of an individual given the availability of need-based products and

simplified purchasing options would go a long way in making life insurance the preferred option. One of the basic needs of a young growing population is that of financial protection against unforeseen circumstances along with

the flexibility to plan for their future expenses. The ability to secure more and more lives by leveraging the available technological solutions can place India ahead of other countries – considering the vast untapped potential.



**Sandeep Bakhshi**  
MD & CEO  
ICICI Prudential Life Insurance  
Company Ltd.

Sandeep Bakhshi is an MBA from XLRI, Jamshedpur and has been with ICICI Group for 27 years.

From 1986 - 2001, he worked at the Delhi Office, in the Project Financing Department, of the erstwhile ICICI Ltd. which was a Development Financial Institution.

From January 2002 to April 2009, he worked with ICICI Lombard General Insurance Company Limited and worked with ICICI Bank Ltd. from May 2009 to July 2010.

He has been working with ICICI Prudential Life Insurance Company Limited since August 2010.



## Expectations of India Inc. from the New Government

**Mr. Atul Joshi**

*Managing Director & CEO, India Ratings and Research – A Fitch Group Company*

In recent times, Indian policy makers have taken significant steps to equip the Indian Capital Markets with a variety of funding options such as REITs, Covered Bonds, Infrastructure Debt Funds and also incremental steps to provide clarity on Securitisation Trusts. However, more enabling measures cutting across disciplines are called for if such measures are to have the desired results.

This paper mainly dwells on the securitisation market and other recent funding options proposed by policy makers over the last few years for Infrastructure Assets, MSME (priority sector loan securitisations), Real Estate (REITs) and Housing Sectors

(Covered Bonds) and why such measures may not see their intended benefits unless significant steps are taken to address bottle-necks.

In order to make instruments issued by securitisation trusts and other funding options as attractive to investors as NCDs issued by corporates are, a comprehensive all-encompassing reforms specific to the securitisation framework is called for. Such reforms need to look at insolvency laws leading to sanctity of security interest and enforcement, accounting laws and taxation regime and legal framework in order to make these funding options attractive to investors.

***Globally policy makers have provided tax benefits to sectors requiring growth capital of which some examples are the Master Limited Trusts and REITs in United States.***



Most countries with robust securitisation markets achieve the purpose of issuing instruments through SPVs/securitisation trusts in the following two ways, which have proved challenging in India:

**Assignment of assets (existing assets) into an SPV which would issue instruments to investors:** This can only happen when transaction costs in the form of stamp duty is not prohibitive. High stamp duty amounting in some cases to 5% of the transaction or asset value becomes very onerous and can make transactions unviable. As an example, an originator looking to assign regulatory assets from the power sector of INR 3000crs would have to pay a stamp duty of close to INR 150crs in order to receive the benefits of the reduced risk profile resulting in a better cost of borrowing against the security of such an asset. In absence of these prohibitive costs, this could have been a beneficial way for the capital markets to fund the ever-widening working capital gap of the power discoms. Assignment of security interest remains a challenge in other sectors such as real estate also.

**SPV as the financial conduit – NBFC criteria of RBI:** Indian issuers face the hurdle of the ‘Principal Business’ criteria laid out by Reserve Bank of India. This test also called as the ‘NBFC Test’ that requires all entities having financial assets which make up more than 50% of the total assets of the company and if the income from financial assets make up more than 50% of the gross income to have RBI approval required for operating as NBFCs. Having to seek RBI approval for creating a stand-alone SPV for the purpose of achieving a funding objective is too cumbersome for companies to consider. Globally these funding structures work as described below:

- SPV would provide a loan to the issuer which would have security of the assets (existing or future receivables) of the issuer. The

loan in turn would be funded by issuing a capital market instrument to a wider investor base. This route is especially effective for future receivables on which charge can be created but as on the date of the transaction do not exist on the books of the company.

The key benefit of borrowings backed by assets assigned into an SPV is that it allows the borrower to benefit from the lower risk profile of such assets. The lower risk profile arises out of the greater predictability of the cash flows from the asset which may be much better than the overall profile of the corporate. This is especially true for entities with assets of varying risk profile such as operating and under-construction toll roads, airports and utilities with stable and under-construction assets where the crystallisation of receivable assets is subject to certain performance risks like road and air traffic etc.

### Securitisation Trusts - Taxation of Pass through Certificates (PTCs):

Earlier the income distributed by trusts was taxed at the investor level. However, the Finance Bill 2013 requires the Securitisation Trusts to deduct taxes on the gross distributable

income before distributing it in case of investors who do not belong to the ‘exempt’ category. The name Pass Through Certificate has become as misnomer as the income is no longer ‘pass-through’. Securitisation Trusts have largely been used for priority sector loan (PSL) securitisations. Now even for PSL transactions it does not find favor with investors given the new taxation norms rolled out in 2013.

Many countries including China most recently have firmed up plans for financing the MSME sector through the securitisation route given the lack of attractive bank financing to this sector.

Globally policy makers have provided tax benefits to sectors requiring growth capital of which some examples are the Master Limited Trusts and REITs in United States. Similar strategies could be considered for Securitisation Trusts to further the cause of ‘financial inclusion’.

At the minimum, PTCs would become attractive only when they have the same taxation regime as NCDs issued by corporates where taxes are paid by end-investors instead of tax deduction by the Trustee given that such income is ‘pass-through’ and not the business income of the Trustee.



**Bankruptcy laws and Accounting norms need to be considered exclusively for Securitisation Trusts:**

The true benefit of securitisation trusts accrues from their ability to ‘ring-fence’ assets away from other creditors of the company. In India, both issues (bankruptcy-remoteness and off-balance sheet treatment) are considered to happen in tandem. Hence, only issuances from SPVs providing ‘off-balance’ sheet funding are considered as also being bankruptcy remote from the Issuer. However, this need not be true if one goes by International experience. A typical example would be Utility Tariff bonds which are issued consequent to legislative approval to recover ‘sunk costs’. In many countries, such SPVs may be ‘bankruptcy-remote’ for the purpose of the bankruptcy laws. However for the purpose of accounting,



depending on whether ‘significant control’ continues to be exercised by the originator, the SPV may or may not get consolidated with the originator. Doing this allows the instruments of the securitisation trusts to have greater acceptance similar to non-convertible debentures issued by corporates and at the same time allow cheaper funding given the lack of access to such ‘bankruptcy-remote’ assets by the other creditors of the company. The ICAI, RBI and the Ministry of Finance may consider forming a committee to examine the global best practices for such transactions and how such transactions can be facilitated to meet the ever-growing need for capital and also come up with new accounting guidelines applicable especially for securitisation transactions.

**Covered Bonds:**

Covered Bonds are issued such that the issuer pays while it is viable; however if it goes into insolvency, the ear-marked assets and cash flows from such assets are available to pay down the bonds.

NHB made a significant initiative with respect to issue of Covered Bonds by Housing Finance Companies in 2012. However,

the success of such an initiative hinges largely on whether assets that are ‘ear-marked’ for bond holders face challenge from other creditors in the event of issuer’s bankruptcy. Countries such as Australia, Singapore, South Korea and Hong-Kong have taken significant initiatives on this front.

This equips mortgage lenders with long-term funding options using covered bonds. This would also mitigate the funding mismatch that exists within Indian financial institutions that borrow short-term and fund long-term assets such as mortgages. This again highlights the importance of more legal clarity on bankruptcy in such specific situations.

One way to create transferable security interest, avoid significant transaction costs and also greater transparency could be to set up a Security Trusteeship company for all mortgage transactions in the country. It must be compulsory for mortgage deeds to be registered in favor of the Security Trustee Company for the beneficial interest of the lender.

- This company will be holding the security in trust on behalf of the lender.
- If the lender changes – read securitised or issuance through covered bonds – the trustee

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simply changes the beneficiary in favor of the bond holders or PTC holder.

### Real Estate Investment Trusts (REIT):

SEBI recently came with REIT guidelines which if implemented are expected to provide alternate funding route to real estate developers. However, the success of this initiative is again dependent on ability to re-jig existing assets into an entity that expects to list itself on the exchanges without

onerous stamp duty implications and greater clarity on taxation norms where the entity holds the assets through a step-down subsidiary.

If one were to draw lessons from the developed markets, REITs enjoy a 'pass-through entity' status subject to REIT adhering to certain regulations. Such a REIT would pass on at least 90% of net taxable income to unit holders. The incidence of tax is thereby on the unit holders and not on trust, which would pay corporate tax only on non-distributed income.

Also, if corporate tax and/or dividend distribution tax is levied at both levels on up streaming of dividend from SPV to REIT and REIT to unit-holders, it may lead to multiple incidence of taxation. An efficient tax regime would be very vital in making this product viable in India.

Absent these clarifications, most initiatives to provide alternate funding routes to corporates may not see the intended benefits imagined at the time of regulation and law-making.



**Atul Joshi**

**Managing Director & CEO  
India Ratings & Research -  
A Fitch Group Company**

Atul Joshi is Managing Director and Chief Executive Officer at India Ratings and Research – A Fitch Group Company.

Previously, Atul was Managing Director and Head of the Business & Relationship Management (BRM) Group for India at Fitch. He has more than two decades of experience in the financial services industry. Prior to Fitch, Mr. Joshi was in charge of the Financial Institutions Group at ING Vysya Bank India. He was also the Parent Account Manager for India at ING Bank NV. Mr. Joshi started his career at ICICI Bank, where he worked for close to 13 years in both global and domestic treasury functions as well as in project finance.

Atul is a double graduate in Economics and Commerce from Mumbai University, and an all-India 12th rank holder in Chartered Accountancy.



## Expectations of India Inc. from the New Government

**Mr. Sandesh Kirkire**  
*Chief Executive Officer,*

*Kotak Mahindra Asset Management Company (KMAMC) Ltd.*

**T**here is a need for a fundamental change of what we expect from the government: From the creator of development and provider of employment; to enabler of development and ensurer of employment. The former approach makes us more bureaucratic, the latter: more enterprising. The former will require us to stand in the queue for milk outside PSU dairy depots in the morning; the latter will make dairies compete to deliver milk at our doorsteps.

Historically, ensuring a competitive

market with a powerful but a limited regulator (who always intervenes effectively but only on the natural violations, leaving the market to price itself), has always delivered products/services more efficiently, innovatively and profitability. The alternative of this is any combination of monopolistic / oligopolistic market, with heavy/little regulatory intervention. In any of the latter combinations, the likelihood of uneven and ineffective wealth creation, distribution and manipulation is high. Such a setup tends to be riddled with economic inefficiency and is prone to

***Digitization of the registration process is needed along with single window service, requiring no more than 4-6 procedures and 10-15 days***

corruption, both of which are detrimental to sustainable growth.

Enterprises in India face tremendous tariff and non-tariff obstacles in for entering the business; for operating the business; or for exiting the business. While there is no perfect day for doing the business, the fact that India rank's 134/189 in the World Bank's 'Ease of Doing Business' Index, puts us way behind even Sri Lanka and Pakistan.

The monotony of this index number hides the fact that it requires 12 clearances before setting up a new Business. Businesses in India have to engage for nearly 33 types of tax payments and related liabilities during the year. The bureaucratic restrictiveness and ideological cynicism towards private enterprise must be toned down. Because, in the end Indian products using expensive, restrictive and yet sub grade infrastructure, cant compete in a global market and still generate employment, fiscal revenues, current account surplus and low inflation. This paradoxical expectation must be fixed.

The result of restrictiveness is that, India, a land of more than 120 crore people had only around 99,000 new startup limited companies in 2012. While Australia, a country of 2.3 crore, saw 185,000 new startups in the same period. So are we to believe that we Indians are less entrepreneurial?

Point is: the next government must see its economic policy in the following principle:

- Does the policy/procedure make it easy for entry into business?
- Does the policy/procedure make operating the business easy?
- Does the policy/procedure make the exiting of the business easy?

Business Environment Estimation					
Rankings (out of 189 countries)	India	China	United States	Russian Federation	Brazil
<b>Overall Ease of Doing Business</b>	<b>134</b>	<b>96</b>	<b>4</b>	<b>92</b>	<b>116</b>
Getting Credit	28	73	3	109	109
Investor Protection	34	98	6	115	80
Registering Property	92	48	25	17	107
Getting Electricity	111	119	13	117	14
Resolving Insolvency	121	78	17	55	135
Trading Across Borders	132	74	22	157	124
Paying Taxes	158	120	64	56	159
Starting A Business	179	158	20	88	123
Dealing with Construction Permit	182	185	34	178	130
Enforcing Contracts	186	19	11	10	121

Source: World Bank

Entrepreneurship at a Glance						
Countries	Tax Payments (Nos per year)	Approx Cost of Construction Permissions( US\$)	New Pvt Startups (2012)	Entrepreneurship Rate (Per 1000 workers)	Working Population (in Mn)	Per Capita (US\$)
South Africa	7	929.1	217,624.0	6.54	33.3	9,384.6
Malaysia	13	1,916.9	45,441.0	2.28	19.9	13,040.1
Brazil	9	4,932.7	53,876.0	2.17	24.8	14,174.4
Singapore	5	10,148.0	31,532.0	8.04	3.9	64,636.9
United States	11	10,802.5	-	-	-	64,685.8
Australia	11	11,231.2	185,009.0	12.16	15.2	84,444.8
Russian Federation	7	15,616.2	442,165.0	4.30	102.8	17,546.3
Germany	9	24,437.4	69,332.0	1.29	53.7	52,328.4
China	7	26,244.6	-	-	-	7,613.8
United Kingdom	8	32,252.1	455,600.0	11.04	41.3	48,866.9
Netherlands	9	45,610.0	49,425.0	4.44	11.1	57,443.4
India	33	49,151.0	99,587.0	0.12	829.9	1,861.5
France	7	121,502.8	121,538.0	2.88	42.2	49,714.8

Source: World Bank (Data 2012)

Any Government it may be, it would have carried the day (and term) if it ensures high market competition. Such a market would imply highest possible labour demand and wages, lowest possible product cost, maximum drive for innovation, and a more suitable economic method of production and distribution.

Therefore digitization of the registration process is needed along with single window service, requiring no more than 4-6 procedures and 10-15 days. Then be it for business registration, land registration, birth registration, car registration or crime registration. Moreover, the government is also a key enabler of access to many natural resources in the country. A transparent and

equitable process providing a level playing field for free competition must be provided. So if it means implementing a transparent and objectively measurable process (like points based allocation system); or through the bidding; either would be a good start. The government must also streamline and propel the already stalled clearances before more long term procedural effects begin to take root.

The DTC and GST are also two eagerly awaited and much delayed initiatives that need to be implemented in right earnest. Providing political leadership in consensus building and getting these initiatives through would be a major achievement for the next government. GST (in discussion since 2000) would

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especially remove the internal tariff barriers and ease the movement of goods. Moreover, a single GST model is what must be pursued rather than settle for half measures.

Wherever possible, the UID based direct cash transfers are to be ensured, thus giving a more surgical delivery of welfare programmes and subsidies. Currently, the explicit and implicit subsidies (such as doling out of Banks, PSUs, Power Distributors etc ) by State and Union governments are estimated to be anywhere between 3-5% of the GDP.

A more targeted delivery of subsidy should reduce the size of the government and its welfare overheads, while giving better delivery of the goods and reduced pilferage (currently govt spends Rs 3.65 to deliver 1 Rupee in Food subsidy). Ergo, over a period of time, the requisite government expenditure would reduce while obtaining a similar level or more by way of social output.

Where the cash transfers are not possible, such as in public education (or for instance in the midday meals), the government must look to deliver its social service goods through private sector deliverers who are competing for the job. There is much to learn about this aspect from the Scandinavian countries in this regard.

Additionally, PSU's engaged in non-strategic commercial activities must be exposed to free competition;

and limitations such as binding labour laws and political appointments must be reduced to the minimum. The professionalization of the PSU is essential else such entities become a huge and repetitive liability on the fiscal balance sheet. Those PSUs that can be divested must be done so with competence. Every non-strategic PSU/Private entity must be able to justify itself in the marketplace by the cost and quality of its product and service; rather than seek political protection from competition or open-ended infusion of public money as capital.

For instance, the bulk of the NPA of more than Rs 2.7 trillion by the Public sector banks would in the end be borne by general citizens of India. The fact remains that the available discretion and monopoly of power within the public/

government sector, coupled with lack of accountability provides a toxic incentive for poor decision-making, bad execution, and misappropriation. This results in massive loss of precious public money that could otherwise be used in more productive purposes.

In the financial arena, the reform of the Pension sector and further liberalization of the Insurance and banking sector is much awaited. The high entry barrier for private sector and FDI investment in these areas must be lowered and entry licenses must be subject to transparency, objectivity and through an open window format. Liberalization and integrating the bond market with currency and derivatives market to make the borrowers and lenders compete is also needed. Additionally, the need for reorganizing the current financial regulatory architecture to the needs of the modern environment (as envisaged by the proposed Financial Sector Legislative Reforms Commission) must be addressed in earnest.

Having said that, government is the sole and primary provider of Law and Order in the society. The economic



cost of prolonged civil and criminal cases; and equally, the economic and time cost of managing the crumbling civic and social infrastructure needs to be addressed in earnest. It is therefore imperative that the Indian Judicial system and police system

be reformed and professionalized to the highest benchmark using the Information Technology.

Finally, the Chinese Leader and the original reformer of the Chinese Economy, President Deng Xio Ping had quipped, "It doesn't matter

whether it's a white cat or a black, I think; a cat that catches mice is a good cat". His was a simple point: pragmatic utility is more important than dogmatic colors. Hope that pragmatism for growth and prosperity prevails.



**Sandesh Kirkire**

Chief Executive Officer  
Kotak Mahindra Asset Management  
Company (KMAMC) Ltd.

Mr. Sandesh Kirkire, is a Mechanical Engineer, and holds a Masters degree in Management Studies from Jamnalal Bajaj Institute of Management Studies (JBIMS), Mumbai University. Mr. Kirkire joined Kotak Mahindra Group in 1994. He has over 24 years of experience in financial services spanning Corporate Finance, Investment Banking and Funds Management.

Mr. Kirkire joined Kotak Mahindra Asset Management Company (KMAMC) Ltd. in 1999 as its Chief Investment Officer (Debt) and took over as Chief Executive Officer (CEO) in May 2005.

Mr Kirkire has been the pivotal force behind KMAMC having grown to be a top 10 player in the Indian Mutual Fund industry, having one of the most diversified and exhaustive product suite across domestic equity and fixed income, international funds, FOF, Exchange traded funds and gold.

Under his leadership, KMAMC has won many awards and accolades including the NDTV Profit Business Leadership award - Fund House of the year 2006; Outlook Money NDTV Profit Best Debt Fund House - 2007 and 2009 and Lipper Fund Awards for Best Bond Fund group - 2006 and 2007.

Mr Kirkire is currently the Vice Chairman of the Association of Mutual Funds in India (AMFI) - the industry apex body



## Expectations of India Inc. from the New Government

**Mr. R Govindan**

*Vice President - Corporate Finance & Risk Management,  
Larsen & Toubro Ltd.*

**N**obody doubts India's potential to be an engine of global growth. However, structural problems causing underinvestment in India's infrastructure are a major impediment. While difficult to quantify, a rule of thumb suggests that India's infrastructure deficit shaves off 2% points of its GDP every year. As against targeted infrastructure spending of USD 1 trillion in the 12th 5 year plan, India may achieve just USD 550-600billion. Half of this is supposed to be funded by the private sector, which has played a major role in infrastructure creation over the last decade. Assuming 25% participation by

the private sector in the 10th & 11th 5 year Plans, USD 186 billion has been committed. Roughly \$40-45 billion of equity investments have been made, which in the current environment are not yielding remunerative returns due to falling GDP growth & rising interest costs. Confidence in governance in India has been affected. Many infrastructural projects are held up due to a multitude of issues. If the new government is not stable and if urgent policy measures are not implemented immediately, the threat of a sovereign downgrade is looming large for India. With stretched government finances and overleveraged private sector bal-

***The GST is India's most ambitious indirect tax reform, If implemented in the right spirit, it will boost revenue collection for the government while cutting business transaction costs***



ance sheets, it has become imperative to attract foreign investment for infrastructure formation.

### Financing Challenges/ Deepening Of Bond Markets

The pre-liberalization financial system was centred around keeping the Government's cost of borrowing low since it was the primary driver of economic growth. Prior to the 1991 reforms, financial repression in India was absolute. Financial household savings were parked at banks, which, in turn, bought government bonds in a process that came to be described as "lazy banking". The total bank financing in India is USD 1trillion, while non-bank financing is about USD 800bn. Excessive reliance on the banking system creates challenges during crisis periods when the banking system becomes dysfunctional. As compared to the developed world, Indian bond markets are less liquid with limited set of issuers. Corporate bonds outstanding in developed countries are around 30-40% of GDP compared to India's 5%. Many deliberations have happened on developing the corporate bond markets but concrete measures are yet to take off. Suggestions include taking measures for increasing investor appetite, facilitating credit enhancement mechanisms & providing tax incentives akin to those in equity markets.

The Indian central government deficit is USD 90bn. Banks roughly raise USD 120bn every year in incremental deposits and over 25% of this is lent to the government due to the SLR mandate. Instead, if India frees up limits for FII investments in G Secs, a substantial chunk of bank deposits can be freed up for infrastructure formation.

Almost 50% of India's financial savings go into the banking system while the balance 50% is channelized into other products such as insurance, pension, equity and gold. Such non-banking financial savings should be directly channelized into infrastructure formation.

Indian infrastructure developers lack liquid markets for monetising such assets. This restricts availability of capital for creation of new assets. Foreign jurisdictions have regulatory frameworks such as Real Estate Investment Trusts & Business Trusts. India currently is working towards developing a regulatory framework for REITs. However, for such frameworks to succeed, tax and stamp duty issues need to be addressed.

A number of measures also need to be taken to allow foreign capital into the country. Currently, there is a withholding tax of 20% on offshore bonds for non-infrastructure sectors as against 5% on infrastructure bonds/loans. However, infrastructure EPC companies still do not seem to be eligible for the lower withholding tax benefit. A high withholding tax in case of offshore bond issuances adds to the costs for the issuer and should be reduced. The bank loans market cannot really cater to the long tenor and large amounts that bond markets offer. Domestic developers should be permitted to exit from construction development projects through FDI infusion so that capital can be churned for further capital asset generation in the country. Re-financing of existing ECBs and rupee loans with new ECBs should be made easier. Given that infra companies have to necessarily establish SPVs for

infra projects, investment into equity or debt of such SPVs should be a permitted end use for ECBs taken by the parent entity. MIFOR swaps should be permitted as an IRS instrument for better management of ECB hedges.

Further, the new Companies' Act mandates all companies that raise funds through issue of debentures to create a debenture redemption reserve (DRR) and also maintain 15% of the monies in low interest bearing instruments or SLR-backed instruments. NBFCs are required to create a DRR equivalent to 50% of debentures or bonds over the repayment term. This is a retrograde step as cost of funds could increase 80 to 90 basis points. Additionally, this will significantly reduce their ability to pay dividends.

### Manufacturing Sector

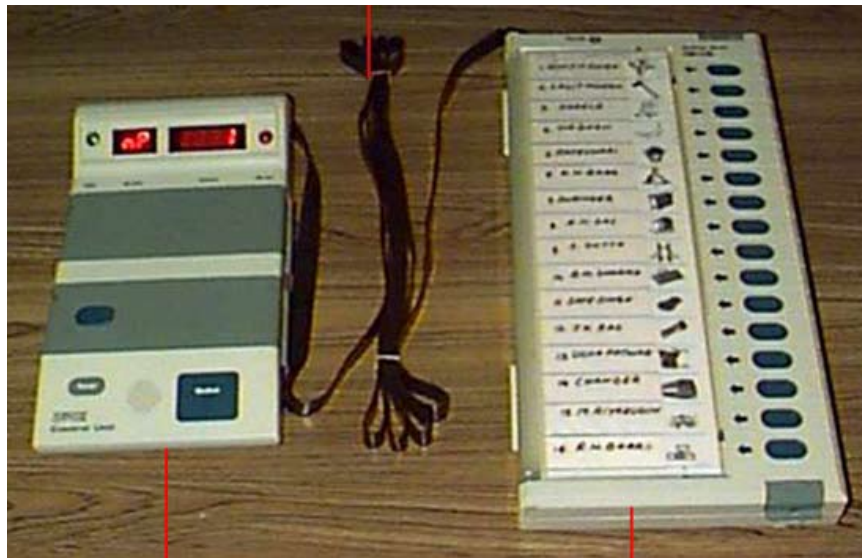
India's lack of manufacturing capabilities is a serious disadvantage to growth. The share of manufactured items in India's exports has reduced from 77% in 2003 to 61% in 2013. India's major non-oil non-gold import items include electronics, capital goods, chemicals etc. All such imports could easily be avoided if India had a cost-competitive manufacturing sector producing a variety of world-class products. Every country that has become prosperous post World War II - be it Japan, Germany, China or the



other Asian tigers – has done so on the basis of a strong manufacturing sector. India seems to be an exception in this regard in trying to migrate directly from agriculture to services without getting into manufacturing. This is likely to be unsustainable. The share of manufacturing sector in the gross domestic product needs to be increased from 15% to over 25%, which can create 90-100 million jobs.

### Land Acquisition

The recently passed Land Acquisition Act aims to satisfy the woes of the land losers and simultaneously provide a systematic framework for acquiring land. However, with higher compensation for land and associated R&R costs, the overall land acquisition cost is expected to rise significantly, forcing companies to reassess the viability of their projects. While the Act lays down the maximum time limit for completing various acquisition steps,



the ability of the concerned authorities to adhere to these timelines will be key for the successful implementation of the act. Moreover, the approach of the states towards land acquisition and the form in which they adopt the Centre’s policy will be critical.

### GST

The GST is India’s most ambitious indirect tax reform, If implemented in the right spirit, it will boost revenue collection for the government while cutting business transaction costs. It has the potential to boost India’s economy by up to two percentage points.

### Agriculture Push

Turning agriculture into an organised business with the farmer as the entrepreneur should be the key. Strengthening is needed at all the levels of the supply chain—inputs delivery, credit, irrigation facility, farmers diversifying, procurement, minimising post-harvest losses, cold storage chains, better processing and marketing techniques, efficient storage and competitive retailing.

### Labour

Inflexible labour laws need an overhaul if India is to create the tens of millions of new jobs it

needs to become a low-cost manufacturing centre. Companies are hiring more contract workers to circumvent these stringent laws, leading to pay disparities and a lack of job security for the unorganised workforce. The challenge will be to set measures acceptable to employers, workers and trade unions.

### Defence

As India continues with a massive acquisition programme to provide its armed forces with the latest and best equipment, it is pertinent to ponder over reducing its extreme dependence on imports by building indigenous capabilities across the entire value-chain – from research, design and development to manufacturing, integration, maintenance and repair. The government being the sole regulator needs to design solutions for what is a tightly regulated monopsony market. The regulator and its companies account for almost all of the limited indigenous production. There are multiple areas that need attention—funding, R&D, taxation, protection of intellectual property, foreign investment and collaboration, the import and export regimes. There is need for a comprehensive review of all of these to create synergies rather than contradictions and an eco-system that stimulates investments in building domestic capabilities across the entire

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supply-chain. Though the recently revised DPP is encouraging, the government is still a long way from achieving its stated objective of broad basing domestic capabilities by including the private sector in defence production.

### Tax & Company Law

Apart from being an instrument of raising revenues, taxation laws play a key role in attaining larger fiscal

objectives like encouraging savings and investment, reducing inequalities of income and wealth, fostering balanced regional development, incentivising exports and small-scale industries. However, tax laws have been amended hundreds of times over the years& hence are highly complex. Billions of dollars in taxes are locked up in long-drawn litigations, particularly in relation to cross border transactions

and transfer pricing issues. India still has an inefficient indirect tax structure due to the cascading effect of multiple taxes on goods and services which affects the cost of products and services. The need of the hour is to ensure that significant tax reforms aimed at rationalizing the current tax structure are undertaken to enhance revenue by broadening the tax payer base and improving transparency.



**R Govindan**  
Vice President - Corporate Finance &  
Risk Management  
Larsen & Toubro Ltd.

Mr. Govindan heads the Finance and Treasury functions, including regional finance and treasury centers outside India. He manages the finance and treasury portfolio of more than a 100 group companies at the policy level. He also oversees the Enterprise Risk Management and Insurance functions for the group.

He has been instrumental in developing the Risk Management Policy under the aegis of Audit Committee. In his current role, he takes care of Capital Allocation, Financial Risk Management and Strategic Investments. He has been a part of many international/domestic benchmark transactions in various sectors for the L&T Group (GDR, QIP, FCCB, etc.)

He has completed his B.Sc. in Statistics from Loyola College, Madras, and completed his Post-Graduate Diploma in Management from IRMA, Anand. He mentors L&Tites under various Leadership Development programs. He represents L&T on various industry bodies and professional committees. Under his leadership, L&T won the prestigious EuroFinance Best Treasury Team Award in 2009. He himself won the Euro Finance Best Treasurer Award in 2013.



## Financial Inclusion Needs Change of Direction

**Mr. V.P. Nandakumar**

*MD & CEO of Manappuram Finance Ltd.*

India will have a new government shortly. What the contours of the new government will be like cannot be predicted with certainty. However, what is certain is, it will inherit an economy in serious trouble. Therefore, getting the economy back on track should be its foremost priority. How can this be done? Many ideas have been put forth about what needs to be done. In this article, I'll focus on one area of concern to the financial services sector where a change of direction is a crying need. It has to do with our quest for financial inclusion.

Financial inclusion emerged as a catchphrase around the time inclusive growth became the national mantra. Buoyed by the consensus that growth

must be inclusive, we went after more causes with "inclusion" tagged to it. Financial inclusion, in this sense, was ripe for the picking. But now that the lustre around inclusive growth has dimmed somewhat, it's time financial inclusion came under the scanner too.

Financial inclusion is the delivery of financial services at affordable prices to the poorest sections of society. While India's banking sector has done well of late, a sizeable section continues to be excluded from even basic banking services. India is home to the second largest financially-excluded population after China with an estimated 135 million such households (or two-thirds of the population). Predictably, rural India fares dismally. Reacting to

***While India's banking sector has done well of late, a sizeable section continues to be excluded from even basic banking services***

this gloomy scenario, our policy establishment went into overdrive, seeking to ramp up the provision of a range of financial services to the poor, such as a no-frills banking account for making and receiving payments, a savings product in tune with their cash flows, money transfer facilities, small loans and overdrafts etc.

### No magic bullet

When an idea becomes a catchy slogan, it acquires an importance disproportionate to its intrinsic worth. In turn, it draws attention, and resources, away from other equally worthy causes. Financial inclusion has become a buzzword, and we're all for it. Implicit in the consensus is the assumption that once boxes representing various measures of financial inclusion are checked, beneficiaries emerge out of the poverty trap. It's rather simplistic, to say the least.

Poverty is an outcome of the interplay of multiple factors working in ways that feed into each other. A root cause, it may be said, is the lack of education and marketable skills which condemns the poor to the lowest occupational rungs. Under these circumstances, a bureaucratic approach that artificially prioritizes financial inclusion, in the expectation that everything else will fall in place automatically, is unlikely to work.

### Destroys value

Besides, there's a good reason why so many of our theoretically well-conceived policy measures have floundered at the ground level. Simply put, a development initiative whose costs are incurred upfront, without assurance of proportionate benefits flowing down the line, is essentially an exercise in value destruction. It's a leaking bucket that loses water faster than the inflow from the tap above. For example, the government can determine that people of a locality lack access to transport which impedes their mobility. It can then choose to promote "in-

clusive mobility" by, say, giving away free motorcycles. The cost is heavy and it's all incurred upfront. Imagine the waste, then, if people who get hold of these motorcycles find they do not have the money to buy fuel, pay for other upkeep, or even know how to ride it.

Likewise, a ham-handed pursuit of financial inclusion destroys value. Regulatory pressures compel commercial banks to incur substantial expenses (not to mention opportunity costs) in extending benefits to the excluded, but who are unable to derive due advantage because other enabling conditions are absent. In December 2012, then Deputy Governor of RBI, Dr. K.C. Chakrabarti, noted that under the financial inclusion drive 150 million accounts were opened, but only 30 million transactions had taken place.

### Revise the roadmap

In this context, there are two approaches to financial inclusion as seen in India. The conventional approach, favoured by the government and regulators, believes in using the commercial banks to deliver cheap and subsidized products to the excluded sections. However, commercial banks are poorly placed to advance financial inclusion because they are burdened by high legacy and HR costs. About

65 percent of a bank's operating cost is taken up by manpower cost, and PSU banks spend up to four and five times more per employee than NBFCs.

Clearly, the optimal solution is to take on board players who can operate profitably at low costs. When your costs are low, you reach break-even earlier. Once profitability is established, the activity becomes self-sustaining. This is the approach pioneered by India's NBFCs, who rely on a low cost model to deliver products and services that may not be cheap, but delivers real value to the customer because it fits his needs, meets his requirements. At this point, financial inclusion goes beyond mere access to financial products and services to inclusion in the wealth creation process. That's why NBFCs are the safer bet when pushing inclusion while banks are better off in a supporting role, say, extending low cost funds, or routing their own priority sector commitments to NBFCs.

NBFCs have a track record of innovation, consistently doing well in areas that banks have recoiled from. Moreover, success was earned the hard way, under the shadow of a discriminatory regulatory regime. What the outcome under a more benign environment would have been can only be guessed at. A hint lies in our aviation and telecom sectors. Air travel in India



was for long the preserve of the elite. It took the entry of a low-cost carrier like Air Deccan to shake things up. In just about a decade, India's private telecom players accomplished the unthinkable,

making mobile telephony affordable to the common man. And it was done without subsidies, thanks to policies that fostered growth and competition.

Likewise, India's NBFCs can po-

tentially rewrite the rules of the game around financial inclusion. Count on them to pull it off without asking for handouts, and without coercion from above.



**V.P. Nandakumar**  
MD & CEO  
Manappuram Finance Ltd.

Mr. V.P. Nandakumar is the Managing Director and CEO of Manappuram Finance Ltd. based at Valapad (Thrissur District), Kerala. The company's origins go back to 1949 when it was founded by the late V.C. Padmanabhan, father of Shri Nandakumar. Its activity was mainly money lending carried out on a modest scale.

Mr. Nandakumar took over the reins of this one branch business in the year 1986 and has since scripted a story of unprecedented growth. Manappuram Finance Ltd. was incorporated in 1992 and, in a short span of time, became the first NBFC from Kerala to get a Certificate of Registration issued by the Reserve Bank of India; one of the very first NBFCs from Kerala to go for a public issue; the first NBFC from Kerala to issue bonus shares in the ratio 1:1 in 2007, the first Kerala based NBFC to receive Foreign Institutional Investment (in 2007), and to obtain the highest short term credit rating of A1+ from ICRA and P1+ from CRISIL.

Today, Manappuram Finance Ltd. is a pan-India presence with about 3,300 branches across 26 Indian states and UTs, and about 18,000 employees on its rolls. The company has Assets under Management (AUM) of nearly Rs.9,000 crores.

Mr. Nandakumar's achievements in business have been well recognised. In January 2014, Business Today identified him as one of India's Top 100 CEOs. Earlier, in December 2013, Business World had listed him among India's Most Valuable CEOs.

Mr. V.P. Nandakumar was born in 1954 and holds a post graduate degree in science with additional qualifications in Banking and Foreign Trade.



## Expectations of India Inc. from the New Government

*Mr. Rajesh Sud*

*CEO & Managing Director, Max Life Insurance*

A couple of years back, few of my friends who had migrated to the West wanted to return to India and be a part of India's growth story. Some of them now thank their stars that they didn't return; others feel there is still hope. While earlier I was strongly backing the second group, today I feel that India must act decisively and quickly to keep the growth story intact and in turn, the faith of its people intact.

India's growth engine has slowed considerably and FY 2014 looks set to be second year in a row with sub 5% GDP growth. For the fiscal year 2006-07 India was the second-fastest growing economy with a 9.4% economic growth rate, second only to

China. Current GDP growth is huge climb down from those levels and it has truly been a lost opportunity to harness the Indian economy's full potential.

As an Indian, first and foremost, one hopes that the electorate delivers a clear mandate and the new government thinks and acts simultaneously to resuscitate the nation's growth mechanisms and clear the overhang of uncertainty. The Government will need to put an effective growth plan in place that will be able to tackle the burgeoning fiscal deficit, tame inflation, maintain a trade deficit level that can be financed by capital inflows and –most important– revive industry's confidence.

***The new Government needs to improve the competitiveness on export and expand into new geographies and substitute import with domestic production***

The net message of all the policy has to be a clear “India is open to business, it subscribes to transparent dealings, it is anti-corruption and it wants to improve the lives of all its citizens but understands that it will require to do different things for different segments and is committed to this happening steadily through a period of time. Most important of all, it will hold itself and its various constituents accountable to its citizens to deliver this continuously.”

On the fiscal side, the following need to be focussed upon

### **Inflation must be restrained**

Food inflation had reached a dizzying height of 16.6 in September 2013. Even though the current WPI has declined to 4.7 per cent due to increased winter supply of fruits and vegetables, it may increase again in the summers. A high inflation rate eats into the disposable income of households and their saving capacity. The new Government must control inflation and encourage household savings. As experience in China has shown, this virtue can truly be the backbone of various capital formation plans that can fuel investment and growth.

The inflation issue is a combination of demand and supply side factors. The RBI has raised Repo rates several times but that is only a temporary mechanism. Supply side reforms are essential for a lasting solution to the problem of inflation. A comprehensive monetary and fiscal policy should be in place to rein in inflation across various components of WPI and CPI.

### **Bring in a new Green Revolution**

About 55% of India’s population still depends on the agriculture sector. At the same time over 9 million farmers have left farming in the last 10 years. It is time for Green Revolution 2.0 in India which would involve adoption



more advanced agricultural inputs such as mechanization, high yield seeds and new irrigation technologies by Indian farmers. There is also a need for investing in knowledge and skill development of farming community. Some of the imbalances such as soil leaching have been caused by government subsidy schemes. There is a need to rationalize use of subsidies. Precision agriculture seems to be a viable solution to optimally utilize scarce resources and build sustainable and profitable agriculture sector. Such efforts on the part of government will result in higher productivity which in turn will help stem the migration from agri-based rural economy to urban centres.

### **Improving Trade deficit**

India’s position in the global economy is showing signs of stagnation and will need to improve considerably. The country has had a high current account deficit for the past few years, which is currently being contained thanks to a revival in export growth and restrictions of gold imports. With the expectations of rupee strengthening in case of a stable government at centre, export growth will require some fiscal support in the form of export credits to neutralize the

impact of high domestic taxes, input inflation and currency impact.

The new Government needs to improve the competitiveness on export and expand into new geographies and substitute import with domestic production. Export of value added manufacturing output needs to be promoted to build a well rounded export basket. The Current Account Deficit that we are facing can be curbed with increased FDI as it is a stable source of long-term capital.

### **Boost infrastructure development**

In the past few years the infrastructure development has slowed due to many challenges such as regulatory delays and challenges in the PPP models and long-term funding sources of infrastructure projects. Many existing projects and existing projects are either facing delays or stalled. 20,000 kms of road projects itself are lying untouched. The Government needs to re look into the PPP contracts and clear the bottlenecks for pending projects.

Life insurance plays a critical role in utilisation of small savings for infrastructure development. To help the sector further enhance this role, the Government has to provide right tax savings support to the long-term



savings instruments and clearly differentiate it from short-term financial instruments. Tax incentives have been a key driver for the growth of disciplined savings behaviour, both in India and other markets.

The effectiveness of such tax policies is clear with regard to shifting national savings to life insurance and promoting long-term savings. An additional tax incentive of Rs.1.5 lakh to life insurance and Rs. 1 lakh for retirement plans could result in significant growth in life insurance industry which will also result in additional inflow of Rs. 90,000 crore in infrastructure and Rs. 2,20,000 crore into government securities by Financial Year 2020.

‘Soft infrastructure’ i.e. education and healthcare is another area which requires attention. Over the past few years enrolment in secondary education has improved significantly but the quality of education remains an issue. Poor quality of education not resulting in jobs for youth could be a cause of social issues. In healthcare, it is not just the quality but also the reach of government healthcare machinery that needs to be tackled by the new government. In fact, hospitalization is one the biggest causes of households just above the poverty line slipping back to below poverty line as they have to avail private medical facilities which they cannot afford.

### Leveraging technology for transparency

India’s business approval process is seen as one of the most bureaucratic and cumbersome. Through a ‘Government to business IT enabled platform’ the new government needs to bring in transparency to business environment.

The Government must put out expected turnaround times for simple services that can be e-enabled. For larger projects, a continuous report progress can be available on a real time basis. Accountability should be fixed

for delay in projects and reasons for delay and consequence management should be transparently reported. Similarly, the ones doing a good job should be recognised and encouraged through financial and non-financial means.

### Opening up FDI

Opening up of FDI avenues should bring in further long-term capital. Some of the announcements of outgoing Government included liberalizing FDI norms in sectors like retail, aviation and broadcasting. On the other side, the budget also announced a hefty 29% rise in planned spending, given the need to spur growth in the context of the current slowdown.

I would want the new Government to implement the long pending Insurance Bill amendment. The proposed amendments include increasing the foreign equity cap to 49 per cent as against the current FDI limit of 26 percent. If this is done it will also bring in domain capital which is of critical importance in this phase of growth of life insurance industry. The bill also includes certain provisions to provide the Insurance Regulatory Development Authority (IRDA) with flexibility to discharge its functions. The overall objective is to support

the reform process which is already underway in the insurance sector to bring back growth in the life insurance sector.

### Long-term regulatory roadmap

The Finance Ministry and the regulators should collaborate with the industry to define a clear regulatory roadmap for BFSI sector for the next decade. Beyond the roadmap, the Finance Ministry should adopt hands off approach and encourage regulators to co-ordinate amongst themselves on topics of common interest such as Banks and Brokers.

Secondly, the Government (Finance Ministry) and the regulators should lead the financial literacy initiative and this will require a systematic and sustained effort to improve financial literacy in the country that will boost efforts of banking, pension and insurance sectors.

The India story is far from over. In fact last few years of low growth gave a reality check to focus on structural reforms in the Indian economy. The country has faced tough economic times earlier and has always managed to steer itself and emerge stronger. If the new Government puts in adequate focus on honestly implementing



policies and reviving projects, then the country will be back in the 'high growth' trajectory. I believe, life insurance industry has the potential to contribute a large part in this revival. It's time to convert India's often quoted and equally lamented 'strong long term potential' into a near term reality and soon!

Rajesh Sud is the CEO and Managing Director of Max Life Insurance, one of the first three private life insurers to start operations in 2001, when the insurance sector was opened to private participation. A founder member at the company, he is committed to achieving the Vision of making Max Life Insurance the Most Admired Life Insurance Company in India.

Over the last five years, Rajesh has led the company through one of the most dynamic periods for the industry. He has made significant contribution as a senior industry leader by shaping industry agenda as member of various committees in industry bodies. He is especially passionate about "customer centricity" and drives this theme across the industry as the Chairman of the Consumer Awareness Committee of Life Insurance Council. Under Rajesh's leadership, Max Life Insurance has become the largest non-bank life insurer in the country having a consistent record of profitable growth for the past four years. The business has won several recognitions under his leadership like the Golden Peacock Award for Excellence in Product Innovation, CII National Six Sigma recognition, the Asia Insurance Industry 'Innovation of the Year' Award, the Gallup Great Work Place Award 2009 and BT-Mercer-TNS Best Companies to Work (7th Rank).



**Rajesh Sud**  
CEO & Managing Director  
Max Life Insurance

Before taking up the role of CEO, Rajesh was responsible for establishing a diversified distribution network for Max Life. He is specially recognised for successfully establishing the most productive 'Agency' in India- as the core channel for the company with strong focus on process, training and productivity and for forging a unique long term bancassurance relationship with one of India's largest private banks.

Prior to joining Max Life Insurance, Rajesh was the Head of Asset Finance business at the largest foreign bank in India, ANZ Grindlays Bank and was seconded as the CEO and MD of the Bank's subsidiary finance company, Esanda Finance and Leasing Ltd. Rajesh started his career with Bank of America and held various positions of increasing responsibility. Rajesh was part of the transition team that managed the successful sale of Bank of America's consumer banking business to ABN Amro Bank and served as the Head of Consumer Banking Sales

Rajesh completed his Advanced Management Program from Wharton Business School, University of Pennsylvania, Philadelphia, USA. He also has a Management post graduation degree in Marketing and Finance from one of India's foremost management schools, Faculty of Management Studies, Delhi University.



## Expectations of India Inc. from the New Government

**Dr. V Shunmugam**

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Recent announcement of the election dates and expectations of participants had already sent the markets on a roll on the assumption that the new government would unleash a slew of economic policies to revive economic growth and carrying the reform and liberalization process to newer heights. Even though, the economy may be recovering from a decade low economic growth levels, high fiscal deficit and inflationary pressure situation, as indicated by the recently released economic data, the question of economic sustainability would continue to linger in the minds of the stakeholders and the domestic and foreign investors alike. Keeping in mind the same,

a downgrade in sovereign credit rating is what the current policy regime had been aiming to avoid with a slew of policies to reduce the twin deficits to the targeted levels, despite the expected reduction in revenues arising out of lowering economic output and the reduction in global demand.

One of the key measures that were taken includes the restrictions on the import of gold which was used largely as a physical means of putting the savings of the domestic stakeholders. Central bank estimates that out of INR 20,037 Billion of gross domestic savings per annum during FY12, more than 60% percent of it had been invested in non-financial asset classes affecting its ability to further fuel

***Efficient and widely participated market would take the economy further in the process of economic liberalization, privatization and globalization process and deliver its benefits sustainably***

growth aspirations of the economic stakeholders and policy regime alike. This highlights the very basic nature of problem faced by the Indian economy- the ability to transform all domestic savings into financial savings especially in terms of market-based asset classes such as shares, bonds and other securities. If the numbers are to go by, gold imports have not only accounted for a large share of the import bill affecting availability of precious foreign exchange for other economic purposes, but also providing the economic stakeholders with increased opportunity to put their savings into non-financial asset classes including gold. Efforts to increase retail investment participation in Indian capital markets have been taken in the past and would have to be continued by the new government in a proactive manner providing critical access to the markets and at the same time providing for a policy



regime that would create liquid and deep capital markets in India. In this regard, an attempt has been made here to highlight few such measures if taken by the new government would provide for liquid and deep capital markets in India.

its mettle in helping various nations including Singapore in providing not only for development of their real estate but also providing for their banking sector to grease the wheels of entrepreneurship aspirations of their respective economic stakeholders. It will also provide for infrastructure companies to raise cheap funds outside India. However, the successful launch of REITs would need certain fiscal measures to induce wide investor participation. According to a CARE report 1 (2013), "REITs are similar in principle to mutual funds except the underlying security would be in the form of physical property. To offer a level playing field with the existing MFs, the tax structure of REITs also needs to be made similar as applicable to mutual funds. However, there is not much clarity on the tax front for REITs at present. Any adverse tax structure is likely to be detrimental to the acceptance of this new product in the market." Relevant questions before the policy makers such as how the regular income of the investors in REITs would be treated? How would the Capital Gains be taxed? Learning from some international experience could offer some guidance for India's fiscal policy. Malaysia, for example, was one of the first countries to develop listed property trusts, encouraging small-

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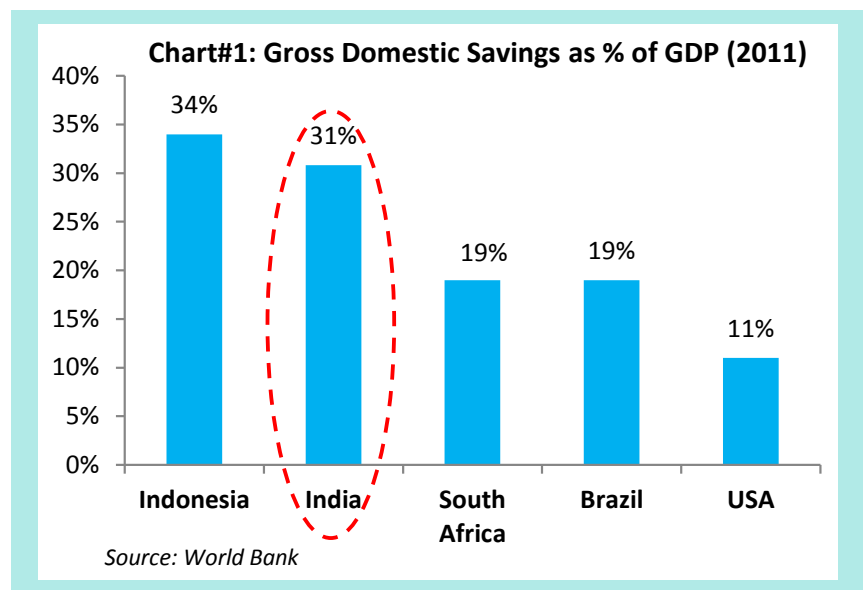


### How to take the current efforts by the government to the next level:

One of the most important non-financial asset class remains the real estate based investments. Such investments are largely made by the economic stakeholders with access to debts or leverage that could enable them access these asset classes or with large funds to commit for a medium to long period in time. In order to increase the access to real estate based investments and thereby enable the economy achieve the growing demand for the same and to enable investors reap the benefits of their investments, it is necessary that these asset classes are transformed into financial asset classes that could be traded in the financial markets. Real Estate Investment Trust is one such financial market asset class which has proved

time investments in the domestic real estate. Under its REIT regulations, the Malaysian government progressively introduced tax incentives to promote its capital market, with an exemption on most income earned on REITs. Apart from this, several other exemptions are also provided by the policy makers including exemption from stamp duty, real property gains tax to promote it as a mechanism to fund such opportunities. Among other countries, Singapore had also introduced similar tax exemptions as incentives for investors and to promote investments in REITs.

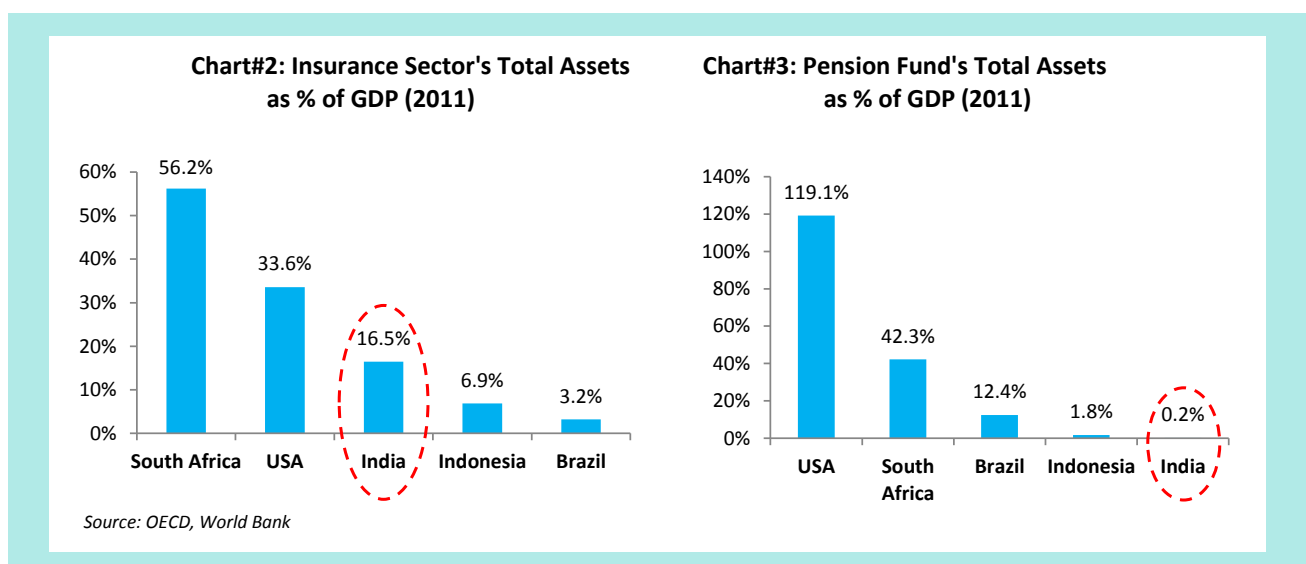
Rajiv Gandhi Equity Saving Scheme (RGESS), a tax saving scheme announced in the Union Budget 2012-13 and expanded in budget 2013-14, is designed especially for the first time retail investors in securities to increase retail savings in market-oriented financial instruments especially in to the top 100 stocks of the national stock exchanges and/or the equity shares of PSU enterprises. Increasing the scope of number of investable stocks while focusing on routing the funds into infrastructure development could be the way forward for the upcoming new government. In addition, similar to the UK's Individual Savings Account (ISA) and Canada's Tax Free Savings Account, the scheme shall be made perpetual and investment limits



in them shall be perpetually revised to reflect the potential income of the stakeholders besides inflation, and the fiscal needs of the nation. When it comes to pensions related such savings schemes, the Roth 401 K of the United States and the Superannuation scheme of Australia are noteworthy in promoting systematic long term systematic savings by the stakeholders themselves using financial instruments that are available for investment by the stakeholders themselves using fiscal instruments which sacrifices a smaller part of the current revenue potential for a larger part of the long-term potential of the stakeholders.

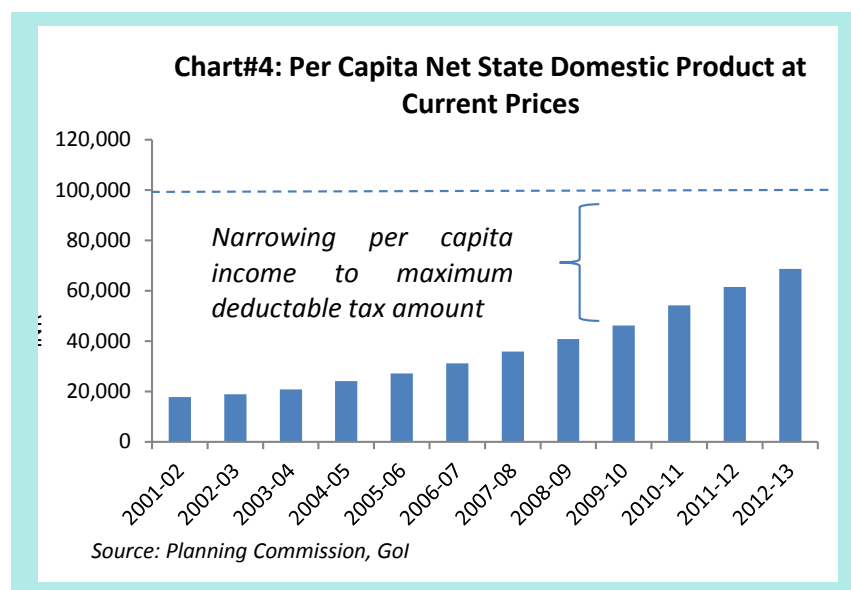
Apart from the deliberate policy

efforts to promote financial savings for the long term economic health of the stakeholders, the pension and insurance sectors have also served for a longer term as a major investment source used by the retail investors. In a country with high domestic savings as percent of GDP (see chart#1), promotion of investment in both these sectors and liberalization of institutions created for the same purposes with stringent risk management and surveillance would help in converting part of household income into financial savings. However, despite a healthy savings rate, on an international comparative scale, India is relatively lower than its counterparts in terms of



assets managed by pension funds in relative GDP terms with a somewhat slightly better amount of assets under management by the insurance sector (see chart#2,3). To add to it, their participation in the capital markets is also restricted to the the respective sectoral investment regulations and lack of financial products that match their investment objectives. In the coming years, India should follow the path of other nations in channelizing long-term fund flow in to capital markets and infrastructure development by further liberalizing/strengthening insurance and pension funds sector and to connect them with funding needs with suitable products such as REITs as described above.

Fiscal Provisions such as 80C shall be dynamic enough to reflect the current economic conditions of the economic stakeholders in India in an effort to promote savings by the economic stakeholders in financial asset classes i.e. investing in India's future economic opportunities. Section 80C was introduced under the Finance Act 2005 providing information for tax deduction from total income in respect of various investments, expenditures, and payments. However, the limit for maximum deduction available under Sections 80C, 80CCC and 80CCD (combined together) has remained INR 1,00,000 since the inception of the Act while the annual average income of households has more than tripled from INR 20,871 to INR 68,757 during 2003-4 and 2012-13, signifying that while the maximum tax savings



bracket has remained constant, income level has increased by about CAGR of 14%.

**Development of corporate bond, currency and other derivative markets:** With increasing need for formalization of India's economy and privatization of large public sector, it is essential that their capital needs be effectively intermediated to increase efficiency and provide asset classes that help them manage their risks in the most efficient in a world where risks are offloaded thinly to non-stakeholders while businesses become increasingly competitive in an increasingly globalized world. With corporate bonds playing a key role in intermediating debt capital efficiently between savers and the user corporates, India needs to have deeper markets with larger issuances and liquid trading of corporate bonds.

Apart from developing the corporate bond markets, efforts towards internalizing the currency derivative markets are much needed in light of the growing interests in trading same in other regulated markets. This is evident from the fact that growth in offshore markets had outpaced the growth of the onshore markets since 2007 (see table#1) largely due to the quantitative easing policies of the west. While growth in Over the Counter (OTC) and Exchange Traded Markets (ETMs) continue to shift gears due to changes in policies, a larger role is being played by strengthening of information and communication technology (ICT) which has helped information to be effectively converged into markets but also that participants have got an opportunity to converge them in real time, fueling USDINR trading in the offshore or other

**Table#1: Offshore and Onshore share of total FX turnover (%) Rank**

CV	2003		2010		2007	
	Offshore	Onshore	Offshore	Onshore	Offshore	Onshore
Brazilian (Real)	79.6	20.4	67.6	32.4	64.7	35.3
South African (Rand)	79.5	20.5	73.9	26.1	74.6	25.4
Indian (Rupee)	53.0	47.0	45.5	54.5	24.2	75.8
Korean (Won)	42.7	57.3	42	58	32.1	67.9

Sources: BIS Triennial Central Bank Survey (December 2013), IMF, FOW Trade calculations

regulated markets that operate during extended hours. With increasing capital flows across the borders, it has become inevitable to strengthen the onshore markets for USDINR to enable stakeholders discover the exchange rates effectively balancing it with domestic fundamentals along with information related global economic fundamentals. Easing of policy restrictions related to institutional participation and incentives for risk management using transparent markets besides setting up accounting standards that eases their participation related reporting requirements while monitoring the risks associated with the same effectively.

Indian capital market has a vast potential to achieve the goal of enhancing financial inclusion by offering investors the opportunities

for creation of wealth and sharing of the same in a more inclusive manner. For this to succeed, introduction of innovative products and services that meet the risk-return requirements of a broader spectrum of investors is needed, while efforts towards enhancing financial literacy should remain the necessary for long term goal for the development of capital markets. Such an effort to be taken by the stakeholder institutions would have to be aided by public investments into it keeping in mind the long-term returns potential. Financial inclusion, apart from being a social responsibility, also promotes business opportunities that are capable of leading growth in overall economy more indirectly and directly in the financial services sector. Also existence of widely participated market not only improves

inclusion by sharing the benefits of growth widely among economic stakeholders but also improves the other process of the markets namely price discovery and risk management. Continued efforts by regulators is needed to achieve inclusive growth, and one way to accomplish that goal is to encourage more retail investors from tier II and III cities to participate in capital markets with appropriate fiscal incentives and development institutions that could help public policy achieve the same. Efficient and widely participated market would take the economy further in the process of economic liberalization, privatization and globalization process and deliver its benefits sustainably across all economic stakeholders and to make the process of economic growth more sustainable in the times to come.

### References:

- <sup>1</sup> CARE Ratings, 2013, "Real Estate Investment Trusts in India Challenges and Impact", pages 1-4
- <sup>2</sup> May 21st, 2012: The positions in the exchanges (both Futures and Options) cannot be netted /offset by undertaking positions in the OTC market and vice-versa. The positions initiated in the exchanges shall be liquidated /closed in the exchanges only; July 8th, 2013: Banks restricted from carrying out any proprietary trading in the currency futures / exchange traded currency options markets.



**Dr. V Shunmugam**  
Chief Economist  
MCX Stock Exchange

Dr. Shunmugam V has a rich global experience in intensive policy matters, developmental economics & research and working in close proximity with policymakers and market regulators. He is a prominent figure in the industry, foreseeing and proposing policy changes for its impending impact on larger business environment. A thought leader and trained macro-economist with a wealth of network across ranks and files in Government, regulators, business, academics, he has expertise in dealing with multiple regulators, markets, products and strategic communication with various industry stakeholders.

In his role as Chief Economist at MCX-SX and at MCX prior to that, he has structured pragmatic policy recommendations based on the foresight about its linkages with various aspects of the economy and its impact on economic stakeholders, investors, producers, savers, intermediaries and institutions, leading to balanced and sustainable growth of the economy. He plays a key role in interfacing with regulators, product development & research, risk mapping and product design. Before his stint in India, Dr. Shunmugam worked with the US Government where he played a robust role of connecting the Governments of India and the US through trade relations, commodity market dynamics, trade & policy matters and facilitating workshops, conferences, and official missions. He also engaged in resolving several non-tariff barriers, helping industries and importers establish appropriate forward and backward linkages in financial markets ecosystem value chain of India.

Dr. Shunmugam has authored several reports, analyses, papers and articles on various subjects related to financial markets, regulation, dark markets, market micro-structure in various media and journals of international and national repute. He is a Ph.D. in Agricultural Economics from Indian Agricultural Research Institute, New Delhi (1997) and M.Sc. in Agricultural Economics (Gold Medalist, 1993). He was selected for Senior Fellowship award under Indian Council of Agricultural Research and also associated with Ford Foundation Research Project on Natural Resource Economics.



## Expectations of India Inc. from the New Government

**Mr. Samir Shah**

*Co-Chair, FICCI's Working Group on Commodities & Managing Director & CEO, NCDEX*

India has come a long way from the years that were dominated by Hindu rate of growth to a phase when we were almost close to a double digit rate of growth. During last couple of years the trend in growth has concerned the policy makers as well as India Inc though we have been striving to resume the growth trajectory. However, our aspirations now extend beyond merely resuming the growth trajectory to aspiring for growth that is not just impressive but inclusive too. The same has been laid down by the government in its agenda time and again. While the XI Five Year Plan speaks of achieving inclusive growth as a priority, the XII Plan document aspires to achieve

“faster, more inclusive and sustainable growth”.

In inclusive growth, everyone contributes and everyone has a share. It prompts all the stakeholders to play a pro active role. One of its implications is guaranteeing remunerative agriculture to the farmers, one of the most important group of stakeholders in the Indian economy. It also suggests assurance of better trade opportunities to the processors, exporters, traders, commission agents and the like. In this context, expectations from the government are focused around initiatives that would help the commodities market develop and flourish in India like other asset classes

*India Inc expects the new government to empower the FMC with statutory powers on par with those enjoyed by the SEBI*



## Primary market reforms in commodities

There are 7000 regulated markets including 2500 main market yards and 4500 sub market yards in India; however, these are not integrated. Disintegrated markets along with supply bottlenecks impede the benefits of a competitive market from trickling down to the farmers. The same can be fixed by a national e-spot marketplace or a unified market platform (UMP) that could enable trade across APMCs in the country. Such an e-spot market can be initially created in a state by introducing unified license to all market functionaries whereupon they can trade from any or all the marketplaces in the state. In the later stage the state level markets could be integrated to form a UMP for the entire country. Such a market operating on a centralized server would enable economies of scale and would not only facilitate quality based competitive bidding and direct payments to the farmers but would also guarantee online collection of cess to the government and real time dissemination of prices to all the stakeholders. It also would help provide short term credit to farmers desirous of storing their produce in the APMC approved warehouses.

NSPOT has partnered with the Government of Karnataka on similar lines and has helped establish a UMP in the state. The Exchange has been entrusted by the government to help out in the mandi modernization drive including e-auctioning and procurement. Rashtriya e Marketing Services (ReMS), the joint venture is a testimony to NCDDEX collaboration with state government helping to usher in the “one country – one market” phase of market reforms in India.



### Amendment to the Warehousing Act

One of the important parameters of primary market reforms is reforms in warehousing. However, electronic credits system is not technically covered by the existing Warehousing (Development and Regulation) Act, 2007 (WDRA) reasoning that electronic credits are not ‘negotiable warehouse receipts’ and the said Act does not provide for manner of endorsement of such electronic credits. Therefore, the government is expected to amend WDRA to include a specific chapter for regulation of maintenance and transfer of goods by transfer of corresponding electronic credits in the electronic registry like COMTRACK<sup>01</sup> irrespective of whether such credits are negotiable or not.

### Forward Contracts (Regulation) Amendment (FCRA) Bill, 2010

As the French proverb goes, “In the councils of a state, the question is not so much, what ought to be done? As, what can be done?”, there is indeed a lot that could be done which actually does not stress on the financial

resources of the government but can be done with prompt initiatives by the industry backed by equally prompt decisions and actions of the government. Enactment of certain pending legislations could make a lot of difference to the business and investment landscape of the country. In this context, the FCRA Bill, 2010 prompts our urgent attention. The size and growth potential of the commodity futures market in India require the presence of an autonomous and strong regulator and an apt regulatory framework. So far FMC has successfully regulated the market within the existing framework and powers given. However, the powers enjoyed by the FMC are far below than required while FMC also stays exposed to judicial challenges for regulatory actions. India Inc expects the new government to empower the FMC with statutory powers on par with those enjoyed by the SEBI. Hence, passing and enacting the FCRA Amendment Bill should be at the top of the government’s agenda.

Currently the regulators of commodities exchanges have no jurisdiction over spot markets, which are regulated by APMC Acts of the respective

<sup>1</sup> NCDDEX has independently developed an electronic system specifically for commodities called COMTRACK®. It is currently being used by NCDDEX for recording of transfers of credits of goods from the sellers to the buyers.

state governments. To develop an efficient commodity market, spot and futures markets should be integrated by placing both under a single regulatory framework. FCRA amendment is expected to take care of this gap as well.

In the context of FCRA amendment India Inc also expects the government to permit options in goods and certain types of derivatives and derivative products like index futures, weather options, etc. Options are any time a better risk management tool than even futures contract. However, prohibition of options in goods and certain types of contracts like index futures, weather options etc. not only stunts the growth of commodity markets leading to the inefficiency but also robs the farmers of their “waiting power” as they resort to distress sale.

While India Inc strives to bring in more innovative and customized products and services in the market, it looks upon to the government for help in increasing the width and depth of the markets. Participation of FIIs and banks and other foreign intermediaries could add a lot of value to the market and the industry expects the government to permit the same in a phased manner. Initially, such participation may be permitted in non-agricultural commodities and may be expanded to agricultural commodities in a phased manner. Also the industry expects the government to provide for corporatization and demutualisation of recognized associations in accordance with the scheme to be approved by the FMC. The new government could also provide for transfer of the duties and functions of a clearing house of an exchange to a clearing corporation.

### **Exemption of commodity exchanges from the Essential Commodities Act.**

A prominent issue that India Inc expects to get resolved from the new



government is the exemption of commodity exchanges from the ambit of the Essential Commodities Act. The Act basically aims to check inflationary trends in prices and to ensure equitable distribution of essential commodities.

The Planning Commission views, “Much higher levels of human development can be achieved even with the given structure of the economy, if only the delivery system is improved.”<sup>2</sup> With rapid globalization and increasing agri production, the Government would require to substantially dilute administered price mechanism and integrate the internal food-grains market with the global markets. The purpose of permitting forward contracts is to provide risk management and to curb speculations. The commodity exchanges have been working towards this and it would be rightful if the exchanges are exempted from the Act.

The state governments have been working to check hoarding. However, they also should be made to realize that where a segment of trade is entirely governed by the central government under a central enactment, the provisions of other enactments should not

come in the way of the former. Also, physical deliveries under futures contract are allowed at only Exchange approved warehouses spread across the country depending upon the commodity. The center for delivery at the time of physical delivery is chosen by the seller. The buyer has to compulsorily take delivery at those centers. It is difficult for the buyer to know in which State he will get delivery and whether that would violate the prescribed stock limits of the State. Also, if different states prescribe different stock limits for the commodities traded on futures market, it would simply difficult to design uniform forward contracts at the national level. Therefore, the Government can rightly consider exempting commodities stored by the market participants in the exchange accredited warehouses for sale/purchase under a forward contract from the application of control orders issued by State Governments and to instruct all states accordingly.

### **Removal of commodities transaction tax (CTT) in Agricultural Commodities**

The Department of Revenue has issued a notification that CTT would be

<sup>2</sup> Planning Commission, 2008, p. 2

levied on all commodities except 23 agricultural commodities. The notification assumes that agri commodities undergoing processing are not agricultural commodities. However, this goes against the definition of “agricultural produce” as given by the Agricultural Produce (Grading and Marketing) Act of 1937. It increases the transaction cost of several agricultural commodities to farmers and traders. Processed agri commodities should be treated at par with basic agricultural commodities. The industry expects that CTT on processed agricultural commodities should be removed as it would adversely impact not just the commodity derivatives market but also the food economy.

### Special exemptions to farmer producer organizations (FPOs) to become members of commodity exchanges

Currently FPOs in the country provide several services like agri input supply, procurement and packaging, marketing, insurance, technical and other services. Allowing FPOs to participate on commodity derivatives exchanges would result in farmers finding better returns for their produce through increased price transparency and visibility accorded by futures trading. It will also provide further depth to the market and may increase the availability of deliverables on the futures platform. Procurement organizations would procure substan-

tial quantities from a single platform as against the current decentralized operations. Hence, FPOs should be granted a special form of membership on futures exchanges by the new government.

### Conclusion

Growth takes place and markets flourish where there is a conducive policy environment along with swiftness of trade and transparency in practices. Hence, commodity market reforms deserve our prime attention. Expectations of India Inc from the new Union Government, thus, stay crucial and the industry expects the government to help plug in the policy gaps while ushering in a business friendly and progressive regulatory regime.



**Samir Shah**  
Co-Chair, FICCI's Working Group on  
Commodities &  
Managing Director & CEO  
NCDEX

Mr. Shah joined NCDEX on 1st March 2013, initially as the Dy. CEO and has been designated as the Managing Director & CEO.

Just before that, Mr. Shah was the Chief Business Officer of the Dubai Gold and Commodities Exchange (DGCX). At DGCX he led the growth of the exchange to make it the one of fastest growing exchange in the world, winning several awards, amongst them were Contract of the Year and the Best Commodity Exchange in 2012.

Shah has two decades of experience in building institutions and market infrastructure. Prior to joining DGCX, he was the CEO of Mumbai-based Universal Commodities Exchange (UCX).

Prior to this, Shah worked at global information company Thomson Reuters for 17 years. In 2010, he was appointed as the Global head of Business Planning and Operations for a new inside-Sales unit at Thomson Reuters called Direct. In 2009, as the Head of Business Operations for Thomson Reuters Asia and a member of the Asian Leadership Team based in Singapore, he successfully transformed the business to focus on customer needs.

In 2006, Shah led Reuters' India operations as the Managing Director for Reuters in South Asia. In this position, he doubled revenue, integrated the Indian Quotation Systems business and merged the India operations of Thomson into Thomson Reuters.

In his previous roles, he led the Treasury and Fixed Income Business for Reuters Asia, and partnered with large global market makers to launch RTFX and RTFI, the dealer-customer FX and Fixed Income Trading Systems in Asia.

Prior to that, as Head of Sales for ASEAN & South Asia for Reuters, Shah developed trusted relationships with several large banking customers helping them in areas of trading systems, Risk Management, and Foreign Exchange pricing.

Shah began his career as an investment banker in Mumbai helping companies unlock value through public offerings and buy-out deals.

He is an MBA in Finance, a Mechanical Engineer and has completed an Advanced Management Program from Wharton.



## Now is the time to deliver!

**Mr. Vikrant Gugnani**

*Chief Executive Officer, Broking & Distribution Businesses,  
Reliance Capital*

As I pen down my thoughts, the Nifty is making new life-time highs at 6,800+ (30%+ since August 2013), FIIs have topped up their 2013 investments of over Rs1.1 lakh crore with an additional Rs13,000cr in 2014 year-to-date and the INR has strengthened from ~Rs68/US\$ to ~Rs60/US\$ (up ~12% since August 2013). However, this has materialized in the backdrop of continued sub-5% GDP growth; absence, or at best, very little signs of any pick-up in India Inc.'s investment cycle and the challenging fiscal situation that the Indian economy is saddled with, which will prevent neither the "Inclusive

Growth" or the "India Shining" phrases to make headlines anytime soon.

So, why are investors lapping up stocks when there has been little to write home about with regards to the India earnings growth story in recent times? The answer to this lies in the exercise currently underway in India and the hopes and expectations which have been built around the possible outcome.

India, the world's largest democracy, is currently in the midst of the world's biggest democratic exercise - its General Elections (2014). And, there are various opinion polls and weighted individual opinions that are floating in the market, which are trying to guess

*I believe, whichever party comes to power, the challenges and issues, to mend and resurrect the economy and people's confidence, will remain the same*

the party and the coalition-combination that will come to power when the final votes are counted on May 16th.

While many may get the political party right but the final seats count wrong, and a handful may get both right, the probability of all of them going wrong entirely at the current juncture seems highly unlikely. This is considering the anti- and the pro- waves being talked about and published across the media (including the very active social media) and also the general conversations between the ‘aam aadmi’ (not the party) at the various nukkads and the paan-waalas.

However, that is not the point here. I believe, whichever party comes to power, the challenges and issues, to mend and resurrect the economy and people’s confidence, will remain the same.

India has been growing below its potential, in fact, much below its potential, over the past few quarters as the GDP growth has failed to cross even the 5% mark in the past 7 quarters and India is all set to register second consecutive year of sub-5% annual GDP growth! While a slow global growth engine over the past couple of years can be blamed only for a limited portion of this slowdown on account of spillover effect, a significant reason of India’s growth taking the backseat has been home-grown. Therefore, what is expected of the new government is exactly what has been not-moving or slow-moving over the past few years.

Thus, what India needs at the current juncture is a prudent mix of fiscal, financial and infrastructure reforms, notwithstanding what the various party stand is on various issues. While reforms like gradual increase in diesel prices, capped LPG usage, FDI in multi-brand retail, State Electricity Board Restructuring Plan, setting up of Cabinet Committee on Investment (CCI) to accelerate investment projects approvals, etc., have been initiated, lack of significant progress on these has clearly impacted India’s growth prospects in recent times.

Thus, apart from further traction on the above already initiated reform processes, it is imperative that India acts quick on certain important areas like the implementation of a nation-wide GST, which will help do away with multiple layers of taxes and would lead to not just better and transparent tax administration but also increased tax payer compliance as the effective tax rate is expected to drop post GST implementation. However, consensus building between the States and the Centre will be an absolutely necessity for the smooth roll-out of GST.

Also, in order to meet India’s capital requirements and keep the trade deficit under check, other measures like continuation of FDI in Retail, hike in FDI limits in Insurance & Pension, Aviation and Defense need to be considered seriously and swiftly, which will lend a helping hand in attracting foreign capital into the country.

The new government may want to consider fast-tracking the disinvestment process to ease the pressure off its balance sheet, which is currently under tremendous stress. This is particularly important considering that the Public-Private-Partnership (PPP) route will have a very important role to play in building India’s infrastructure set-up, be it Roads, Railways, Ports, Airports, Power, etc., the spending towards which is pegged at

~US\$1 trillion. Again, there is greater co-ordination required here between the centre and the state governments, especially to smoothen the process of land acquisition, environment clearances and raw material sourcing for projects.

There is also an urgent need to address the country’s lagging Logistics sector as India’s supply chain constraints have been one of the key contributors of stubborn inflation in the country. Notably, high trade deficit and high inflation, consequently leading to rupee depreciation, are deterrents for the RBI to cut interest rates, which is an important lever to revive economic growth.

Further, amidst the changing demographics, the basic requirements of an average Indian has clearly moved beyond the basic roti, kapda aur maakaan to attractive job opportunities, higher-better-accessible education system, quality health facilities, richer food options, stronger security – both local/national, efficient transport systems, etc. And in order to achieve this, it is imperative that the new government has corruption-free and better governance systems in place, which accords clearer responsibility and accountability of the various tasks/projects that need to be carried out in the larger interests of the community and the society at large.



It is also important to note here that irrespective of the Party at the centre; the most important thing expected from the new government is the “political will” to execute, without which

India could continue to languish at around the 5.5-6% growth rates at best. While a strong pick-up in the global growth engine may add a percentage point or thereabouts, it is important

that India unleashes the domestic potential by resting on the strengths of its 120cr+ population, which in fact could insulate the Indian economy from global turmoil in future tough years.



**Vikrant Gugnani**  
**Chief Executive Officer**  
**Broking & Distribution Businesses**  
**Reliance Capital**

A Chartered Accountant; Vikrant Gugnani is the CEO of Broking and Distribution Businesses of Reliance Capital.

Vikrant, in his current role, leads these businesses that offer a single window for transacting in a wide range of asset classes such as Equities, Commodity Derivatives, and Gold Savings. These businesses also offers an array of financial services including Wealth Management, Investment Banking, Money Transfer; and distribution of financial products such as IPO's, Mutual Funds, and Insurance (Life & General). All the products and services in these businesses are offered under the brand name of Reliance Money, owned by Reliance Capital.

Prior to the current role, Vikrant was the CEO of Reliance Capital Asset Management Ltd. in India. Under his leadership, the assets under management for the AMC grew from \$3 billion in 2005 to \$22 billion in 2009 and profits (post tax) grew from \$3 million to \$ 28 million during the same period.

His vision of involving Tier 2 and 3 towns in India into the capital markets on the one hand and taking the organization global on the other, helped the AMC in expanding its reach in India and abroad - offices in over 300 cities in India; subsidiaries in Singapore, UK, Malaysia and Mauritius - and increasing the customer base from 700,000 to over 7.5 million.

Vikrant has over 20 years of financial industry experience and has worked with global companies like Citibank and S. B. Billimoria & Co. (currently a member of Deloitte Haskins), where he successfully transitioned the India investments business from a manual distribution model to a comprehensive automated wealth management model.

Vikrant has received various accolades – both at the national and international forums. Some of these include:

February 2013: ET NOW Awards For Retail Excellence (BFSI) - CEO of the year.

July 2012: Asian Confederation of Businesses – ‘Thought Leader Award’ for Mastering Change in a Hyperactive Business Environment. This award is in recognition of remarkable progress in initiating changes in its process; remarkable for others in the same industry to follow the example

May 2009: Asian Investor magazine - “25 most influential people in asset management in Asia”

January 2009: Asia Asset Management (an Asian Pensions & Investments Journal) - CEO of the year (2008) for India.



## Expectations of India Inc. from the New Government

**Mr. Gaurav Kapur**

*Senior Economist & Senior Vice President,  
Royal Bank of Scotland N.V.*

### **New government should initiate structural reforms to deliver higher, sustainable and equitable growth**

With the new government due to take office in June, the task of spurring economic growth and curbing inflation which would entail structural reforms, will be the main priority. Growth momentum remains weak and even though a recovery is now in sight, it would be slow at best. The process of recovery can be derailed by risks emanating both from the global as well as local factors. Despite weaker growth, CPI inflation has remained high and persistent, eroding the value of the Ru-

pee, denting consumer spending and negatively affecting investment activity. More alarmingly, after recent years of high inflation, decline in financial savings, low business confidence and stalled investment activity, even the potential rate of growth of the economy has come down. The Reserve Bank of India (RBI) estimates that the potential rate of real GDP growth may have come down to below 6% from 8-8.5% between 2005 to 2008. The next 5 years would therefore be crucial to address economy's structural problems in order to realize the long-term growth potential, with a focus on job creation in order to fully utilize the advantage of a demographic dividend.

***Boosting farm productivity through higher investment in irrigation and technology would be the key to meet the rising demand***

### Reviving investments to address infrastructure gaps

The revival of investment activity, particularly in the infrastructure sector would have to be accorded utmost importance by the new government. Addressing the infrastructure bottlenecks is not only necessary for higher growth with low and stable inflation, it is also crucial for inclusive growth and poverty alleviation. A recent World Bank study finds that in order to close the infrastructure gap vis-a-vis the requirements, India is required to make the investments between US\$1133 billion to US\$1726 billion over the period of 10 years (2011-2020). Sector wise, power sector would require the highest investments from US\$375 billion to US\$468.8 billion followed by transport including roads, telecom and irrigation. The Public Private Partnership (PPP) mode should remain the preferred route for developing infrastructure.

### Improving the investment and business climate

Establishing a better investment climate is essential for reviving private sector investment activity, especially in the manufacturing sector. IMF in its recent India report pointed out that the sharp deceleration in investment activity over the last 4 years, is only partly explained by macroeconomic and financial variables like higher interest rates. Rising policy uncertainty, delays in project approvals and implementation and supply bottlenecks, particularly in the mining and power sectors, are also prominent reasons behind stalled investment activity, as per the IMF report. Therefore in order to kick-start private sector investments, the overall business climate in the country has to be improved. That would essentially involve reducing the cost of doing business, curbing inflation, policy predictability particularly on taxation and reducing supply bottlenecks. In case of natural resources, moving to

market based pricing and allocation of natural resources would make the process more transparent and attract investment. Easing strict labour regulation and addressing skill shortages should also be considered in order to create a conducive investment and business climate.

### Reforming the farm sector for low and stable food inflation

Another major macro-economic challenge in recent years has emanated from double-digit food inflation with a significant spill over into non food and non fuel inflation. That in turn has led to rising costs for businesses through higher wage and interest costs. Although food production has increased steadily, barring reversals in 2009-10 and 2012-13, this has not reflected in a softening of food prices in any meaningful manner. Reforming the farm sector, should therefore be the second major priority for the new government and here a gamut of reforms are required.

Boosting farm productivity through higher investment in irrigation and technology would be the key to meet the rising demand. Reducing administrative inefficiencies in food distribution by amending the APMC Acts and curbing the role and number of middlemen between end consumer

and the farmer and improving logistics, is another set of reforms for effectively curbing food price spikes. Allowing for greater market pricing of farm produce and limiting the pace of increase in minimum support prices (MSPs) combined with productivity linked increases in rural wages, is another set of complementary reforms. And finally, developing storage infrastructure and promoting food processing industry, to ensure stable food prices by reducing wastage.

### Fiscal consolidation via subsidy regime reform and implementation of GST

Public finances have been characterized by high fiscal deficits driven by untargeted subsidies, growing pressure for social expenditures, low tax-to-GDP ratio and a narrow tax base. While fiscal consolidation has been pursued over the last two fiscal years, with some reduction in fuel subsidies, the quality of consolidation does not provide for a sustainable reduction in fiscal deficit in the medium-term to 3% of GDP. Reforms are therefore needed to accelerate fiscal consolidation but without sacrificing growth. For that the foremost requirement is the implementation of the GST regime, which would boost growth by reducing tax distortions and creating a single market for goods and





services. Improving tax administration and implementing DTC, are the other key reforms on the revenue side. Reforming untargeted subsidies is equally crucial via targeted transfers which have beneficial impact for growth and income distribution.

### Curbing inflation through a simpler monetary policy framework with a clear objective

With high inflation a key impediment for reviving growth, the task of reducing inflation in a sustainable manner would be best served by giving the RBI a clear mandate to target inflation. That would help in improving the effectiveness of the monetary policy. Dr. Urjit Patel committee on strengthening the monetary policy framework, has recommended adoption of a formal inflation targeting (IT) regime, based on the national level CPI. The RBI continues to adopt the essential elements of this new



monetary policy framework with the explicit aim of bringing headline CPI inflation down to 8% by January 2015 and further to 6% by January 2016. The new government should support this effort from the RBI and accord the central bank greater operational autonomy.

### Ensuring Current account deficit does not widen sharply

External vulnerability has been reduced as seen in the sharp contraction of the current account deficit and exchange rate stability, the focus of the new government should be on ensuring that the CAD remains around

a sustainable of 2.5% of GDP. That would entail enhancing competitiveness of exports, reducing the fiscal deficit, encouraging financial savings to curb demand for gold and further rationalization of oil imports by explicitly linking local fuel prices to global crude oil prices.

In conclusion, implementation of an all encompassing reform package would be the key to creating a more conducive environment for achieving higher levels of growth along with low and stable inflation over the medium-term. The new government should aim to set in motion such a reforms package in the first 100 days of its assuming charge.



**Gaurav Kapur**  
Senior Economist &  
Senior Vice President  
Royal Bank of Scotland N.V.

Mr. Gaurav Kapur is the Senior Economist and Senior Vice President at the Royal Bank of Scotland N.V. in India. His experience at the bank dates back to November 2000 when he joined the bank's economics research team as Associate Economist. Prior to joining the bank he served a year at the Indian Council for Research on International Economic Relations as a Research Assistant.

His academic background includes an undergraduate degree in Economics from Delhi University, a Graduate degree in Economics from Delhi School of Economics and a Post Graduate Certificate in Business Management from XLRI, Jamshedpur.

His area of work involves tracking the evolving macro-economic environment with special focus on the financial markets. His key responsibility is to provide strategic advice to bank's senior management and various businesses and to bank's clients. He is also involved in the management of country risk and sovereign ratings at the Global Country Risk Team of the RBS Group Plc. In this role he is responsible for country ratings and review of macro-economic risk environment for Australia, South Korea, New Zealand and India.

He is regularly quoted in the financial media, both print and television. He has been a member of the RBI experts committee for the review of the national household inflation expectations survey and represents the bank at key industry chambers.



## Expectations of India Inc. from the New Government

**Mr. Avinash Kulkarni**

*Executive Vice President , SBI Capital Markets Ltd.*

**W**ith the elevated level of expectations from the new government in the current state of affairs in the country, one would not envy the job of the new government. However, even in the time of uncertainty, the main agenda for the new government is well defined i.e. revitalising growth through good governance.

Restoring the country's growth to the level of 8-9% will require massive push for creating infrastructure. 12th five year plan estimates investment to the extent of over \$1 trillion in infrastructure. The domestic sources of funds are known to be grossly inad-

equated to meet this huge requirement of funds. The new government needs to assure the investors that it is keen to act as a facilitator of fresh foreign investments both in terms of FII and FDI and should not be seen as targeting them for aggressive tax collections. This needs to be done by focusing on broad policy framework instead of micromanaging the foreign flows.

India is considered to be one of the most difficult countries for starting the business. Planning commission estimates that around 70 clearances are required to get the business going in India. This, in addition to multiplicity of direct/indirect taxes, act as a real

*In the area of agriculture, there is a consensus among experts to dismantle Agriculture produce marketing committees (APMCs). This will result in better compensation for the farmers*

dampener to project India as an investment destination. While substantial effort has been made to create legislation like GST and DTC, the new government needs to work on arriving at a political consensus on these issues. Some studies suggest that implementations of GST/DTC alone increase the GDP growth by about 1%. A transparent, systematic, and nondiscretionary policy framework along with sound business regulations and consistency in approach can position India as one of the most attractive emerging market destinations. Single window clearance approach, as introduced in many emerging market countries, needs to be seriously examined by the new government.

Importance of adequacy of power cannot be over emphasized for sustainable growth. The electricity Bill, 2003 envisaged power to everyone by 2012. Quite a few initiatives have been completed/contemplated to address the known shortfalls like lower utilization of capacities, distribution losses and thefts, right pricing of power to consumers, etc. However, much need to be done in these areas. Considering thermal power as a major source of power, irregularities in coal allocations and subsequent government response have made it almost impossible to run a new power plant profitably. While majority view is in favour of privatization of Coal India, considering the current political scenario, only administrative actions directed to increase mining and to improve efficiency of operations seem feasible. It is expected that the government will take necessary steps to ensure adequacy in supply of coal to encourage investment in this sector.

The new government will need to set its priorities right in allocation of limited financial resources. It faces a challenging task in meeting large capital requirements of PSU banks in order to comply with Base III norms.



This is critical at a time when banks are facing difficult situation both in terms of profitability and asset quality. A holding company structure for banks was envisaged for PSU banks in budget 2010, but the idea does not seem to have taken off. The similar holding company structure can also be considered for other PSUs to improve efficiency. This can be done by transferring the holding in PSUs from their parent ministries to a holding company which would run independently by a board of professionals. The Government may have to take a hard look in continuing their interest in sectors like airlines and hotels.

New initiatives to encourage manufacturing to grow in scale and size should be taken on a priority basis. This will create new jobs and also enable the country to reap benefits of demographic dividend. In the area of agriculture, there is a consensus among experts to dismantle Agriculture produce marketing committees (APMCs). This will result in better compensation for the farmers.

The government has to increase productive spending in sectors like health care, education, water and sanitation etc. and it may explore PPP model for building social infrastructure. While financial sector reforms, Legal reforms, Labour reforms are ea-

gerly awaited; issues related to Defense, Subsidies, Intellectual Property also need to be addressed.

The new government has a challenging task for containing twin fiscal and current account deficits which are major cause for concern for ensuring a stable economic environment. While large part of the current expenditure is sticky – salaries, pensions, and interest payments – cutting unproductive spending on subsidies, mainly on fuels such as kerosene and liquefied petroleum gas, would be necessary. Additionally, the challenge will be to carry the financial burden of populist economic schemes that has been established -- like the National Rural Employment Guarantee Act (NREGA), and the National Food Security Bill, which are too popular for the new government to scrap. The cost of this burden will be felt in the years to come since government's reduced productive spending has a multiplier impact on the economy. The new government should must aim to reverse this trend and raise the government's productive spending. Inflation has remained stubbornly high. No sooner the new government takes office, the most important economic indicator requiring immediate action will be inflation

The list is endless. The task before

the new government is enormous. Many of these issues will require political consensus and corporates expect that the government will engage with other parties in a positive and constructive manner. Attempt to en-

gage with state government for clearances on large projects will have to be made. What is expected from the new government is to take a few administrative actions which have demonstrative effect. A few small steps

in right direction will build a positive sentiment. Some morale boosting announcements from the new regime, strengthening the optimism already generated would, of course, be welcome.



**Avinash Kulkarni**  
Executive Vice President  
SBI Capital Markets Ltd.

Mr. Avinash Kulkarni is Executive Vice President and Group Head of Capital Markets group at SBI Capital market Limited. Prior to this, he was Head of Equity and Commodities Markets Department at SBI Treasury. He joined the Bank in the year 1983 and since then has held various assignments spanning over 30 years in the area of Credit, International Banking, Treasury, Retail Operations and Investment Banking. He was also posted as Head of Bank's Durban Office in South Africa with responsibility of Business development and Client Relationship.

In his extensive service with the Bank he has had the opportunity of working in Metro and Semi Urban areas, primarily in the state of Gujarat. He has handled large Corporate Credit and Equity investments both from buy and sell side. He has represented the bank on the boards of various Companies viz, India Ideas.com, Financial Planning Corporation of India, SBICAP Trustee Company Limited etc.



## Expectations of India Inc from the new Government on Economic Policy

**Mr. R. Sridhar**

*Senior Advisor, TPG Capital, L.P.*

**D**ecelerating output growth marked by volatile investments and stubbornly high inflation in consumer prices are the key macro-economic challenges confronting the new government.

Investment activity is under quite some strain as optimistic forecasts of real returns to projects are not being realized due to generalized inflation pressures. After a period of robust earnings growth from the early 2000s till the second half of the last decade, real returns to investment projects are slowing down because of the pick-up in aggregate price level pressures. The recent industrial relations disputes in the manufacturing sector in India can

also be understood in this broader context as labor input costs are under strong upward pressure.

The gridlock in the policy making environment - marked by contested moves on taxes, tariffs, pricing of natural resources and environmental regulations - has also contributed significantly to dampening investment confidence. The gridlock and regulatory obstacles have also, in some notable cases, resulted in key projects not coming to commercial operations stage, thereby also resulting in financial distress for borrowers; and further compromising asset quality in lending institutions such as banks, already under pressure due to the swings in

*Two decades after economic reforms were initiated, it can now be understood that the foundation of economic policy making in India is quite weak*

the economic cycle. Increasingly and unfortunately, though, this gridlock in the policy making environment is highlighted as the single biggest impediment to the revival of economic growth in the country. As a corollary, people assume that once a new decisive government is in place, high economic growth will automatically resume in India.

Nothing could be farther from the truth. Two decades after economic reforms were initiated, it can now be understood that the foundation of economic policy making in India is quite weak. This weak foundation would come back to haunt India's medium-term economic prospects even if some or many of the "gridlocks" are opened in the next year or so.

At the global level, it does not seem like the world economy would turn around in a strikingly strong manner in 2014 / 2015 to provide a noticeable lift to emerging economies such as In-



dia by way of net exports growth. In any case, India has long run an external trade deficit and the support from net exports has never been a stand-out feature. The on-going slowdown in China, nascent recovery in the US but still weak economic prospects in the euro zone and Japan do not bode well for any noticeable external impetus to the local economy. Probable geo-political developments, such as in Ukraine, eastern Europe and east Asia, may also add to the overall uncertainty on the economic front going forward.

In this overall backdrop, there cannot be a stronger case for strengthening the foundation of economic policy making in India, so as to insulate the domestic economy from external developments and keep it on the right growth path.

The advent of a new government right in the midst of these challenges possibly affords a good opportunity for laying such a strong foundation.

### Key Questions

Many fundamental economic questions have remained unanswered in the past two decades, glossed over in the euphoria of high growth in the first half of the 2000s. These relate not only to the

"politics" and the ideological preferences of those in government – these will drive the spending and tax revenue policies of the party and the government in power.

More fundamentally, the questions also relate to the institutional arrangements which should govern policy-making in the modern global economic environment. Specifically, for instance, Indian economic policy makers still – more than two decades after embarking on reforms in 1991 - do not seem to appreciate the fact that monetary policy and fiscal policy are two distinct arms of economic policy; and to the maximum extent possible, the monetary policy making arm should be independent of the fiscal arm and should have the autonomy to work towards a clear economic objective.

Quite simply, the rule governing institutional arrangements at the higher echelons of economic policy making should be: the power to spend the money and the power to create money should be housed in statutorily separate, independent institutions.

The power to spend money rests with the government and the party in power.

The power to create money rests with the central bank.

Where these two powers reside in the same entity or even where they reside prima facie in separate entities

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but are de facto exercised by a single entity ie the government, it is a recipe for macro-economic instability – of the kind India is experiencing now.

Unfortunately, though, Indian governments treat the central bank as just an appendage to finance the gaps in their spending and revenue budgets. They do not seem to recognize that monetary policy is a powerful macro-economic tool that, if employed with integrity, independently and carefully to produce stable prices, can significantly advance the national priorities of stable long-run economic growth and increasing levels of employment.

Therefore, some key fundamental questions which should find clear cut answers in a new government are:

- How big should the government’s spending commitments, meaning subsidies, deficits be?
- What should be the government’s tax and revenue policy?
- Do we have a national policy on tariffs / user costs for key infrastructure such as power, roads, water, transport fuels, gas etc?
- How to plug the overall spending gaps in the national budget?
- What is the role of the Reserve Bank of India in that process? Or,

should the RBI have any role at all in the process?

- Does RBI have any objective at all with respect to the macro-economy?

Healthy, long-run growth in India depends on finding clear answers to these very fundamental questions. If India does not answer these questions, we will have a repeat of what has happened in the past decade – booming activity both in real and financial sectors for some time ( as was the case between 2001 and 2007 ) and then followed by a bust (as has been the case between 2008 and now)



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- MSME Financing
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