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Report by

INDIA

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Note: This report is subject to restricted circulation and press embargo until the end of the first session of the meeting of the Trade Policy Review Body on India.

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I. INTRODUCTION

1. The Indian economy is the second fastest growing economy among the large economies of the world today. In terms of purchasing power parity (PPP) GDP, India is the fourth largest economy after the US, China and Japan. India's share in world GDP (PPP) basis has increased from 4.3% in 1991 to almost 6% in 2005. The World Bank has reported that India has been in the top 10% of all countries in growth performance since the 1980s.[1]

2. Since the mid-1990s the growth rate in agriculture has dropped to 2% compared to the earlier trend rate of 2.5-3.0 percent. The growth in 2003-04[2] was 10% but it came down to 0% in 2004-05. The growth rate went up to 6% in 2005-06 and the advance estimate for 2006-07 puts the growth at 2.7%. In contrast to the sharp fluctuations in agriculture, industry and services have continued to grow steadily. They have been the twin engines driving the overall growth of the economy. The services sector grew at an average rate of 9% in the 1990s contributing nearly 60 percent of the overall growth of the economy. It continues to maintain impressive growth and has recorded, in the last three years, a growth rate of 9.6 per cent, 9.8 per cent and 11.2 per cent respectively. The industrial sector is also expanding rapidly. The sector revived in 2002-03 and its growth rate accelerated to 7.4 per cent in 2003-04 and to over 9 per cent in the next two years. Industrial growth is estimated to be 11 per cent in 2006-07. The growth rate of manufacturing has shown a steady acceleration from 7.8 percent in 2003-04 to 8.7 percent, 9.1 per cent and 11.3 percent respectively in the next three years.

II. INDIA – FUTURE GROWTH PROSPECTS

3. The Indian economy has grown at an average growth rate of about 6% since the initiation of economic reforms in 1991.[3] However, in the three year period 2003-06, the growth rate has been 8.6% showing signs that the economy has cleaved from the past and has entered a phase of higher growth.

4. There exists strong evidence to believe that the economy is being propelled by strong fundamental growth impulses which would sustain in the years to come. These impulses stem from the strengths exhibited by the economy.[4]

(a) Strengths of the Economy

(i) A more open Economy

5. The Indian economy in 2007 is far more open to the external sector than it was fifteen years ago. Table 1 presents a few indices for comparison.

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[1] World Bank: India Inclusive Growth and Service delivery: Building on India's Growth. (29 May 2006) available at http://siteresources.worldbank.org/SOUTHASIAEXT/Resources/DPR_FullReport.pdf.

[2] Indian fiscal year begins on 1 April and ends on 31 March in the next year. A year such as 2000-01 refers to the period 1 April 2000 to 31 March 2001. The period 2003-06 starts on 1 April 2003 and ends on 31 March, 2006.

[3] This section draws from Arvind Panagariya: Transforming India; October, 2006 available at http://www.columbia.edu/~ap2231/Policy%20Papers/Transforming%20India%20Panagariya.pdf.

[4] Adapted from: Shankar Acharya: India's Growth: Past Performance and Future Prospects (November 2006) available at http://www.tcf.or.jp/data/2006120607_Shankar_Acharya.pdf.

Table 1: Towards A More Open Economy

	1990-91	2005/06
Peak Import Duties (manufactures)	200% plus	12.5%
Import Controls	Tight, detailed	Negligible
Trade (goods)/GDP Ratio (%)	14.6	32.7
Current Receipts/GDP(%)	8.0	24.5
Software Exports ($ billion)	Nil	23.6
Worker Remittances ($ billion)	2.1	24.6
Foreign Investment ($ billion)	Negligible	20.2
Foreign Currency Reserves (*$billion, as on March 31)*	2.2	145.1
Debt Service Ratio (%)	35.3	10.2

Source: RBI, Annual Report, 2005/06, except for first two rows.

6. This openness has empowered the Indian economy to become more competitive internationally. For instance, the automobile components industry and the generic drugs industry are in the process of becoming important players in the global market. The growing international competitiveness of the Indian economy is reflected in the steady growth of Indian exports, including services exports.

(ii) A growing "middle class"

7. A survey by the National Council for Applied Economic Research, New Delhi estimates that about 100 million people now live in households with annual incomes between Rs. 200,000 and Rs. 1 million (approximately PPP$ 20,000 to 100,000) compared to about 15 million in 1990-91. This would grow further in the years to come. The aspirations of the growing middle class would provide a strong domestic demand stimulus to the economy.

(iii) The Demographic Dividend

8. According to most population projections, the share of the working age population in the total population will continue to rise for the next 30 years or so. These demographics point to an augmented supply of labour and savings. These demographic trends have also helped raise household savings from 15-16 percent of GDP in the late 1980's to 22-24 percent in recent years.

(iv) Strong and Competitive Corporate Sector

9. The growth in the industrial sector has hitherto been with low levels of FDI, which is reflective of a strong indigenous entrepreneurial sector. A modernizing capital market; an increasingly liberal and competitive environment for investment, trade and production; a wealth of entrepreneurial talent and sustained economic growth has spawned strong new companies and supported the expansion of the aggressive among the existing. The World Bank has pointed out "After 1996, [Indian] companies started reinventing themselves. By 2002, companies had substantially restructured financially and had raised production efficiency and quality while lowering costs. Starting in 2003, companies resumed investing in new capacity with a noticeable pick-up in momentum in 2005".[5] Net profits as a percent of net sales of 1000 listed companies have increased from 4.5% in 2001-02 to 8.9% in 2004-05.

[5] World Bank: India Inclusive Growth and Service delivery: Building on India's Growth. (29 May 2006) page 104.

(v) Increase in Savings and Investment rates

10. These increases indicate that the supply capacity of the economy is being significantly enhanced thus creating a potential for future growth. Gross domestic savings have increased significantly over the recent years. Gross domestic savings as a proportion of GDP increased from 23.5% in 2001-02 to 32.4 per cent in 2005-06. There has also been a sharp rise in the savings of the private corporate sector for four years in succession. The private corporate savings rate in 2002-03 was 4.2%. The private corporate savings rate for 2005-06 (as per quick estimates) has been placed at 8.1%.

11. Gross Fixed Capital Formation (GFCF), as a percent of GDP (at constant 1999-00 market prices) increased from 22.5% in 2000-01 to 26.7 % in 2005-06.

(b) Major Challenges to Growth

12. The Government recognizes the major challenges that have to be effectively addressed for realizing the high-growth potential outlined above.

(i) Infrastructure deficit

13. Growth in the infrastructure sector has not been commensurate with the rapid economic growth experienced by India over the past decade. This has created a structural imbalance which, if not addressed quickly and effectively, can impair the growth potential of the country. The Government has taken concerted action to repair this deficiency.

Power

14. The power sector has been radically restructured with the enactment of the Electricity Act 2003. This Act replaced the three legislations of 1910, 1948 and 1998 and provided a comprehensive framework for reforming the sector. It built on the experience in the telecommunications sector and introduced competition by permitting the entry of the private sector. The Act fully de-licensed generation and freely permitted setting up of captive power plants. Only hydro projects involving a capital cost in excess of the cost limit notified by the Central Government under the provisions of Section 8 of the Electricity Act, 2003 require concurrence of the Central Electricity Authority. Distribution licensees are free to undertake generation and generating companies are free to take up a license for undertaking power distribution.

15. The second major set of reforms is the States signing Memoranda of Understanding (MOU) with the Central Government. These MOUs cover *inter alia* issues such as consumer metering, energy audit, control of theft and setting of tariffs by the State Electricity Regulatory Commissions (SERCs). The Electricity Act, 2003 provides that the SERCs shall adopt tariffs through a transparent process of bidding in accordance with the guidelines issued by the Central Government. This approach to tariff determination, which is a radical departure from the cost-plus approach, is expected to encourage private sector investment. Government issued the guidelines for competitive bidding for determination of tariff for procurement of power by distribution licensees on 19 January 2005. These steps are expected to take the power sector forward. Efficiencies are expected to accrue with the increase in competition. Competition with the private sector in the market place would also have a salutary effect on the public sector entities.

16. The Tenth Plan (2002-07) capacity addition target of was 36,956 MW at the time of the Mid-Term Appraisal. The likely achievement is expected to be around 23,250 MW, which is 63% of the

target in the Mid-term Appraisal. While there is a shortfall vis-à-vis the targets, the shortfalls are lower than in the earlier Plans.

17. An Inter-Institutional Group (IIG), comprising senior representatives of the financial institutions and the Ministry of Power, has been constituted to especially focus attention on fast-track power projects, which could be taken up for early commissioning and could achieve early financial closure. 16 private sector power projects having a total capacity of about 7,320 MW have achieved financial closure and another 12 projects with a total capacity of 12,000 MW are being monitored by the IIG for facilitating early financial closure.

18. Recognising the fact that economies of scale leading to cheaper power can be secured through the development of large size power projects, the Ministry of Power, the Central Electricity Authority (CEA), and the Power Finance Corporation are working in tandem for the development of some projects under the tariff-based competitive bidding route. The Ultra Mega Power Projects, each having a capacity of 4,000 MW, would also have scope for expansion in future. These projects will be able to meet the power needs of a number of States through the regional and national grids.

19. An All India power grid also called the "National Grid", is envisaged to be developed in a phased manner - first by integrating a cluster of Regions and subsequently, by progressive and full integration of all the Regions by 2012. The total inter-regional transmission system is planned to increase from its present capacity of 11,450 MW to about 37,150 MW by 2012.

20. A Scheme of Rural Electricity Infrastructure and Household Electrification was introduced in April, 2005 for providing access to electricity to all rural households over a period of four years. At present, only 44 per cent of the rural households are electrified. The services of Central Public Sector Undertakings (CPSUs) have been offered to the States for assisting them in the execution of rural electrification projects as per their willingness and requirement.

21. The Government is encouraging the use of hydro and wind energy sources which do not rely on fossil fuels and avoid carbon emissions. India has an estimated hydro-power potential of more than 1,50,000 MW. A study by the Central Electricity Authority (CEA) has identified 399 potential hydro projects with an aggregate capacity of 1,07,000 MW. Preparation of pre-feasibility Reports (PFRs) of 162 schemes with an aggregate installed capacity of 47,930 MW has already been completed by the CEA.

Ports

22. Congestion at the ports due to capacity constraints hampers the swift movement of goods. In a world of complex supply chains and just-in-time inventories, this can inflict a cost premium and disadvantage the economy. Significant progress has been made in reforming the port sector of the country. 100% FDI has been allowed in the port sector. Ennore Port situated on the Coromandel coast of India about 24 km north of Chennai Port, is the 12th Major Port and the first Corporatised Major Port in the country. Private Sector Participation (PSP) has been enhanced by following the "landlord port" model, which implies that operational activities of the port are increasingly transferred to the private sector through contractual agreements. In India, PSP has been introduced in the form of a Build-Operate-Transfer (BOT) model. The National Maritime Development Programme, formulated by the Department of Shipping, envisages an investment of over US$13.3 billion for increasing the capacity of ports to bring them up to globally competitive levels.

23. Investments in the ports sector have taken place on a substantial scale. This will be further spurred by institutional reforms in the coming years. At present, 13 private or captive projects with a capacity addition of about 47.60 MTPA and an investment of about Rs.26.62 billion have been

completed/made operational, while 24 others with a capacity addition of around 100.68 MTPA and an investment of Rs.79.10 billion are at various stages of evaluation and implementation.

24. The reforms carried out in the port sector have borne fruit. Port efficiency has improved as evidenced by the fall in average turnaround time from 5.1 days in 1999-2000 to 3.5 days in 2005-06. In container terminals in India, the average crane movement per hour is 22 moves per hour per crane which compares favourably with the movements for other ports in the region.

Airports

25. The rapid expansion in civil aviation over the past few years has resulted in a severe capacity constraint being faced by the Indian airports. This has led to performance inefficiency and large wastages.

26. The international airports in Delhi and Mumbai are being modernized and upgraded through private sector participation. It has been estimated on a preliminary basis that capital investment to the extent of Rs.79.61 billion and Rs.61.31billion will be required for Delhi and Mumbai airports respectively over a period of 20 years in 4 stages of 5 years each. These estimates do not include the cost of likely relocation of some of the assets and removal of encroachments. An 'in-principle' decision has been taken to modernize Chennai airport also through the joint venture route.

27. Construction work at greenfield airports of international standards at Hyderabad and Bangalore is in progress. The two airports are likely to be operational by the middle of 2008. 'In-principle' approval has already been granted to set up a similar greenfield airport in Goa and build new international terminals at Ahmedabad and Trivandrum. State Governments have been encouraged to set up greenfield airports with private sector participation. Proposals to set up greenfield airports in Navi Mumbai, Kannur in Kerala and Pakyong near Gangtok in Sikkim are under consideration. An international greenfield airport has already been built and is operational in Kochi.

28. The Airports Authority of India (AAI) is also considering the development of airports in the non-metropolitan cities. AAI has decided to develop and modernize 35 non-metro airports in the country. The Committee on Infrastructure has approved the report of Task Force for the development of 35 non-metro airports. Development of airports in NE Region will be taken up by AAI on a priority basis.

29. A proposal is under consideration to set up an Airports Economic Regulatory Authority (AERA) to fix, review and approve the tariff structure for aeronautical services and monitor pre-set performance standards at Indian airports. The Authority would be expected to ensure a level playing field for all categories of airport operators and also oversee and deal with the natural monopoly and the common user/carrier segments of airports.

30. The government has adopted a liberal approach in the matter of grant of traffic rights under bilateral agreements with various foreign countries. During the recent past, several new Air Services Agreements were initiated/signed based on modern practices in the civil aviation sector.

31. The tourist charter guidelines have been significantly liberalized in 2004. All airports in the country have been opened to international tourist charter flights. Recently, the government has decided to liberalize the tourist charter guidelines further.

Roads

32. The Indian road network, the largest in the world aggregating 3.32 million km, consists of 65,569 km of National Highways, 1,28,000 km of State Highways, 4,70,000 km of Major District Roads and about 26,50,000 km of other District and Rural Roads.

33. Though the National Highways account for only about 2 per cent of the total length of roads, they carry about 40 per cent of the total traffic across the length and breadth of the country. Considering the importance of the National Highways and the rapid increase in traffic, the Government has taken up the National Highways Development Project (NHDP), the details of which are given in the Secretariat Report.

34. The substantial completion of NHDP PhaseI, i.e. the Golden Quadrilateral connecting the four metropolitan cities of Delhi, Mumbai, Chennai and Kolkata, calls for a shift in emphasis to corridor management – the technique of managing the highways to deliver maximum throughput in terms of speed and traffic volume, while minimizing operational cost and enhancing road safety. The concept of corridor management is being applied to the completed sections of NHDP through operation and maintenance (O&M) contracts. The scope of work, *inter alia* includes road maintenance, road property management, incident management, traffic management and engineering improvements.

35. Government has set ambitious plans for the upgradation of the National Highways in a phased manner in the next few years as below:

- 4-laning of 10,000 km (NHDP Phase III) including 4,000 km already approved.
- Accelerated road development programme for the North Eastern region.
- 2-laning with paved shoulders of 20,000 km of National Highways under NHDP Phase V.
- Development of 1,000 km of expressways under NHDP Phase VI.
- Development of ring roads, bypasses, grade separators, service roads, etc. under NHDP Phase-VII.

36. As a matter of policy, the Government has decided to take up future phases of NHDP proposals mainly on a PPP basis. Implementation of projects through construction contracts will be only in exceptional cases, where private sector participation is not possible at all. Preparatory work has begun in consultation with the Planning Commission for seeking government approvals for the enhanced scope of NHDP.

37. The Special Accelerated Road Development Programme in the North Eastern Region (SARDP-NE), framed for improving road connectivity to remote places of the region, envisages 2/4 laning of about 3,251 km of National Highways, and 2 laning /improvement of about 2,500 km of State Roads and of 1,888 km of roads of strategic importance. This will also ensure the connectivity of 34 district headquarters, out of a total of 85 which are still not connected, to the National Highways in the eight North-Eastern States.

Railways

38. The Indian Railways, the world's second largest rail network under a single management, has been contributing to the industrial and economic development of the country for over 150 years. Of the two main segments of the railways– freight and passenger, the freight segment accounts for roughly two thirds of revenues. Within the freight segment, bulk traffic accounts for nearly 95 per cent, of which about 50 per cent is coal.

39. The high density network, connecting the four metropolitan cities of Chennai, Delhi, Kolkata and Mumbai, including its diagonals, has got saturated at most locations. The Mumbai-Delhi and Mumbai-Howrah routes already have very high capacity utilization. The Ministry of Railways have sanctioned the construction of two Dedicated Freight Corridors on the Eastern Route (Ludhiana – Son Nagar, 1,280 km) and on the Western Route (JNPT-Tughlakabad/Dadri, 1,483 km) at an approximate cost of Rs. 300 billion. An SPV named Dedicated Freight Corridor Corporation of India Limited (DFC-CIL) has been formed to implement the project. Studies on 4 other corridors, viz. East-West, North-South, East-South and South-South are proposed to be conducted in 2007-08.

40. The reform programme embarked upon by the Indian Railways for enhanced business orientation of the organization includes development of fully computerized cost accounting organized on business lines. The new accounting system would support existing government reporting requirements and provide activity/service based revenue and cost data. Policy initiatives for the introduction of competition in certain sectors, like the movement of containers and concessioning of loss-making branch lines, have been taken up as a part of the programme. The programme also includes simplification of procedures to improve customer interface, provision of freight forwarders and private freight terminals.

Public Private Partnerships in infrastructure

41. The Government of India is actively encouraging the PPP model in view of the advantages that it offers in terms of cost savings, access to specialized expertise and proprietary technology, sharing of risks with the private sector and leveraging its own share in infrastructure investments. To accelerate and increase PPPs in infrastructure, two major initiatives have been taken by the government: (a) provision of viability gap funding; and (b) setting up of a Special Purpose Vehicle (SPV), viz. the India Infrastructure Finance Company Limited (IIFCL) to meet the long term financing requirements of potential investors.

42. IIFCL was incorporated on 5 January 2006 with a paid up capital of Rs. 100 million and an authorized capital of Rs. 10 billion. Apart from its equity, IIFCL will be funded through long term debt raised from the open market. There are many infrastructure projects which are financially viable but, in the current situation, face difficulties in raising resources. It has been proposed that such projects in specified sectors – roads, airports and tourism, be funded through a financial SPV. The SPV would lend funds, especially debt of longer term maturity, directly to the eligible projects to supplement other loans from banks and financial institutions. The company would fill the gap for long term infrastructure finance, which the banks are not in a position to address owing to concerns relating to mismatches in assets and liabilities.

(ii) Fiscal deficit

43. Public Finance, both at the Centre and in the States, had deteriorated progressively since the mid-1990s. The combined fiscal deficit of the Centre and the States, which was 9.4% in the year of the economic crises (1990-91), dropped to 6.3% in 1996-97 before creeping back to 9% in 1998-99. The fiscal deficit remained at over 9% until 2002-03. Since 2002-03 a distinct downward trend can

be perceived, both in the fiscal deficit and the revenue deficit, indicating progress in fiscal consolidation.

44. Fiscal imbalance has been addressed by the enactment of the Fiscal Responsibility and Budget Management (FRBM) Act 2003. The Act mandates the Centre to reduce the fiscal deficit to 3% of GDP and to completely eliminate the revenue deficit by 2008-09. 24 of the 29 States too have enacted fiscal responsibility Acts accepting similar obligations – a fiscal deficit of 3% of the Gross State Domestic Product and zero revenue deficit by 2008-09.

Table 2: Fiscal Indicators – Centre and States combined

Year	Fiscal Deficit (FD)	Revenue Deficit (RD)	RD/FD
	% of GDP		
	Combined for Centre and States		
1990-91	9.4	4.2	44.6
1995-96	6.5	3.2	48.8
2004-05	7.5	3.7	48.9
2005-06 (RE)	7.5	3.1	41.5
2006-07 (BE)	6.5	2.2	33.6

Source: Reserve Bank of India, Annual Report 2005-06 Table 1.47.

45. Progress in fiscal consolidation has been satisfactory in the post-FRBM period. The fiscal deficit of the Centre as a proportion of GDP has come down from 6.2 per cent in 2001-02 to 3.6 per cent in 2006-07. Since FRBMA mandated a reduction in revenue deficit as well, gradual reduction in revenue deficit together with the reduction in fiscal deficit resulted in a decline in the proportion of revenue deficit to fiscal deficit by 22.7 percentage points in three years. The proportion of borrowed funds applied to assets creation, therefore, increased to 43 per cent in 2006-07 . Robust economic growth and improved performance of the manufacturing sector continued to maintain the revenue receipts, particularly the tax revenues, buoyant through 2002-03 to 2006-07. Gross tax revenue of the Central Government recorded an average annual growth of 18.8 per cent, higher than the rate of growth of GDP (at market prices), which averaged 12.5 per cent during this period. The gross tax-GDP ratio, which had stagnated at 8-10 per cent range, increased to 10.3 per cent in 2005-06 (provisional) and is expected to improve further to 10.8 per cent in 2006-07.

46. In the Budget estimates for 2007-08, total revenue receipts of the Central Government are projected to be Rs. 4,864 billion and the revenue expenditure to be Rs. 5,579 billion. Consequently, the revenue deficit is estimated at Rs. 715 billion which is 1.5 percent of the GDP. The fiscal deficit is estimated at Rs. 1,509 billion which is 3.3 percent of the GDP. The country is thus expected to be on course to achieve the FRBMA targets.

(iii) Low Agricultural Growth

47. Agriculture in India constitutes the backbone of the rural livelihood security system since it provides employment to about 58.5% of the work force (2001). The total workforce in the agriculture sector rose from 185.3 million in 1991 to about 234.1 million in 2001, an increase of about 26%. This 234.1 million included 127.3 million cultivators (with some land holding) and 106.8 million landless agricultural labourers. According to the National Sample Survey Organisation's survey of the 59th round, the average monthly per capita consumption expenditure of farm households across India was Rs. 503 in 2003. Endemic hunger (i.e. chronic under nutrition), is high both in families without assets like land or livestock, as well as in families with small land holdings without access to irrigation. About 81% of Indian farmers are small and marginal farmers with holdings of 2 hectares or less. Out

of 120.8 million operational holdings in the country, 98.9 million are small and marginal, as per the agricultural census 2000-01. The average size of land holdings has reduced from 2.28 hectares in 1970-71 to 1.57 hectares in 1990-91. The estimate for the average size of land holdings for 2002-03 is only 1.06 hectares. At the beginning of the new millennium, 260 million people in the country did not have incomes to access a consumption basket, which defines the poverty line. Of these, 75% were in the rural areas. It has to be noted that India is home to 22% of the world's poor. Agricultural wage earners, small and marginal farmers and casual workers engaged in non-agricultural activities, constitute the bulk of the rural poor.

48. From the foregoing it would be clear that growth in agriculture is imperative to reduce poverty and inequality in the country. Since the mid-1990s the growth rate in agriculture has dropped to 2% compared to the earlier trend rate of 2.5 -3.0 percent. In order to provide inclusive growth and to dissipate social tensions, not only does this vulnerable sector of the economy need special care and protection, the pressure on land also needs to be relieved by providing alternative avenues of employment in manufacturing and services to the millions joining the agricultural workforce every year. This is the reason why India's agricultural tariffs are comparatively high in comparison to its non-agricultural ones and also of its high expectations in the negotiations in NAMA and Services of providing substantial market access in the developed markets of the world.

49. The government has taken several steps to address the problem of agricultural stagnation. The long term strategy as spelled out in the National Agriculture Policy seeks to promote sustainable and equitable growth based on the efficient use of resources and conservation of soil, water and bio-diversity. The policy goals are to achieve a growth rate of more than 4% per annum in the agriculture sector during the 11th Plan period (2007-12) and thereby ensure food and nutrition security in the country.

50. In order to reform agricultural markets, State Governments have been advised to amend their respective legislations to promote competitive markets in association with the private sector so that farmers can get the best prices. To facilitate the free movement of agricultural goods, the Essential Commodities Act is proposed to be amended to remove existing restrictions on trade of agricultural commodities within the country. Modern terminal markets for fruits, vegetables and other perishables in public private mode are being promoted to link the farmers directly to the markets. Further, a nationwide information network has been established through electronic connectivity to provide quality market feed back and prices to farmers. Rural infrastructure projects like the creation of irrigation facilities, rural electrification and rural connectivity are being revamped through different programmes and initiatives taken by the Government. With an improvement in rural connectivity and irrigation potential, the farmers would be able to get a remunerative price for their produce, which will in turn lead to productivity gains in agriculture.

51. A number of legislative, institutional and administrative initiatives have been undertaken in the past few years for broad-basing agricultural development. A major problem faced by the small and marginal farmers is access to institutional credit on equitable terms. It has been estimated that in the large state of Maharashtra, over 55% of the farm households are in debt. Mechanisms for risk mitigation are poor or absent. Hardly 10% of the farmers are covered by crop insurance. An unfortunate consequence of the constellation of hardships faced by small farm families is the growing number of suicides among farmers. In order to address these issues, a comprehensive credit policy had been announced by the Government in June, 2004 for doubling the flow of credit to agriculture in three years. The goal of doubling farm credit has been achieved in two years. The target of Rs. 1,750 billion set for 2006-07 will be exceeded and is likely to reach Rs. 1,900 billion. From April to December 2006, 5.33 million new farmers have been brought into the institutional credit system. For 2007-08, a target of Rs. 2,250 billion as farm credit and an addition of 5 million new

farmers to the banking system, has been announced. The government has also appointed a committee to examine all aspects of agricultural indebtedness. The committee has held wide ranging consultations across the country and is in the process of finalizing its recommendations.

52. In order to strengthen the institutional mechanism for delivery of credit to the rural populace, whose chief occupation is agriculture, the government is proposing to ask the Regional Rural Banks (RRBs), which are an arm of the nationalized banks, to open at least one branch in the 80 hitherto uncovered districts of the country. In addition, the following measures are also under consideration, viz. to extend the Securitisation and Reconstruction of Financial Assets and Enforcement of Securitisation of Interest (SARFAESI) Act to loans advanced to RRBs, to permit RRBs to accept NRE/FCNR deposits and to recapitalize in a phased programme, the RRBs which have a negative net worth.

53. In order to complement the activities on the credit front, the government has constituted the National Rainfed Area Authority for preparing a perspective plan for holistic and sustainable development of rainfed farming areas. The National Horticulture Mission has been launched for promoting agricultural diversification to high value crops and scientific post-harvest management beneficial for the farmers. The National Fisheries Development Board has been established to provide focused attention to the development of fisheries and acquaculture.

54. Programmes like watershed development in rainfed areas, expansion of irrigated areas along with efficient water resources management, agro bio-diversity and environmental protection, agro-forestry, harnessing of traditional knowledge, a regionally differentiated growth strategy for food and nutrition security, introduction of schemes for the development of allied sectors like horticulture, improvement of livestock, and fisheries, generation and transfer of technology, adequate and timely supply of quality inputs, protection of plant varieties, integrated pest management, etc. have been initiated by the government. Emphasis has been laid on enhancing investments for the development of irrigation, rural warehouses and marketing infrastructure as well as agro-processing.

55. Agriculture extension is being revamped to provide decentralized and demand driven extension support by way of new institutional arrangements for technology dissemination in the form of an Agriculture Technology Management Agency (ATMA) at the district level. Other key extension reforms include convergence of line departments, multi agency extension strategies, group approach to extension, gender strategies, and concerns and sustainability of extension services. Integrated Pest Management (IPM), which encompasses cultural, mechanical and biological pest control techniques with minimum dependence on chemical pesticides, is also in progress.

56. With these interventions, it is expected that the agriculture and allied activities sector would be able to achieve a growth rate of about 4% per annum.

(iv) Skill deficit in manpower

57. While India's young demographic profile has the country favorably placed in terms of manpower availability, talent supply shortages are emerging. This is disconcerting, especially for the knowledge services sector, which over the past few years has emerged as a significant growth engine with demonstrated gains in terms of exports and employment. Research has shown that so far, only a tenth of the global addressable market for these services has been tapped. With its early lead and strong fundamentals (demographics, economics and expertise), India is best positioned to take advantage of this opportunity. Yet the unsuitability of a large proportion of the talent pool in the country could lead to significant lost opportunities. The NASSCOM-Mckinsey Report 2005 indicates that there will be a shortfall of about 500,000 suitable professionals (representing an opportunity cost

of US$ 10bn) by the end of the decade and in the absence of corrective action, this gap will continue to grow. However, if current trends are maintained, the IT-ITES sector (IT-ITES alone of the knowledge sector) will need an additional 1 million plus qualified people in the next 5 years and will generate exports of US$ 86 billion in FY 2012. If the country is to capitalize on the huge opportunity in this sector and other areas of knowledge services, what is needed is a major reform at all levels of education. Clearly, substantial expansion and radical reform of the education sector are called for to ensure that the quality and numbers of professionals needed by the country are met.

III. DEVELOPMENTS IN TRADE POLICY AND CONTINUOUS LIBERALISATION OF TARIFFS

58. India had removed all quantitative restrictions maintained earlier on account of balance of payment reasons in a progressive manner, culminating in the completion of this process in March, 2001. The remaining restrictions maintained on account of security, health, safety and public morals etc. have also been reviewed and restrictions on more than 150 tariff lines at the 8-digit level have been removed subsequent to March 2001. At present, India maintains quantitative restrictions only on items necessitated on account of security, health, safety, environment and public morals permissible under Article XX and XXI of GATT.

59. Export restrictions have largely remained unchanged since 2002. Currently, 171 tariff lines at the 8-digit level are subject to export restrictions. This excludes Special Chemicals, Organisms, Materials, Equipment and Technologies (SCOMET) items.

60. India's average applied tariff on non agricultural products was 24.5% during 2003-04, which has now come down to around 10.1% during 2007-08 as per the announcements made in the Union Budget on 28 February, 2007. In order to take one more step towards comparable East Asian rates, the Finance Minster while presenting the Union Budget for the year 2007-08, announced a reduction in the most frequently occurring high tariff (also known as "peak tariff" in the Indian Budget document) for non-agricultural products from 12.5 per cent to 10 per cent. In addition, he announced several other duty reductions. Duties on most chemicals and plastics have been reduced from 12.5 per cent to 7.5 per cent. The duty on seconds and defectives of steel has been reduced from 20 per cent to 10 per cent. All coking coal, irrespective of the ash content, has been fully exempted from duty. Customs duty on polyester fibres and yarns stands reduced from 10 per cent to 7.5 per cent. Also customs duty on raw-materials such as DMT, PTA and MEG has been reduced from 10 per cent to 7.5 per cent. Duty was brought down on cut and polished diamonds from 5 per cent to 3 per cent; on rough synthetic stones from 12.5 per cent to 5 per cent; and on unworked corals from 30 per cent to 10 per cent. The general rate of import duty on medical equipment has been brought down to 7.5 per cent. Duty on sunflower oil, both crude and refined, has also been reduced by 15 percentage points.

61. These reductions were over and above to those made in January 2007, when the Government had announced a wide-ranging reduction in tariffs. In January 2007, import duties on capital goods, project imports, metals and specified inorganic chemicals were reduced by 2.5 percentage points and, in some cases, by 5 percentage points. Duties on some edible oils were reduced by 10 to 12.5 percentage points.

62. The peak tariff has been slashed from 25% to 10% from 2003-04 to 2007-08, which is a reflection of the radical unilateral tariff liberalization carried out by India. This has provided real and substantial additional market access, to all of India's trading partners without attaching any conditions of reciprocity.

63. In terms of dispersion of tariffs, only 2.21% of the current tariff lines are above the average applied rates of 10.1% for non-agricultural tariffs in 2007-08, indicating that the duties on the bulk of India's non-agricultural tariff lines remain moderate to low. Around 8.4% of the tariff lines are equal to or below 5%. The average rate of tariff would be even lower if one took into account the exemptions available under several notifications issued by the Ministry of Finance.

64. Therefore, in the period since the last Trade Policy Review, India has not only maintained but speeded up the momentum of autonomous tariff liberalization.

65. An important policy initiative for export promotion has been the scheme for the Special Economic Zones. The Special Economic Zones Act, 2005 was enacted with a view to instill confidence in investors and signal the Government's commitment to a stable SEZ policy regime thereby generating greater economic activity and employment through the establishment of SEZs. The SEZ Act, 2005, supported by SEZ Rules, came into effect on 10 February 2006 providing for simplification of procedures and for single window clearance on matters relating to the Central as well as State Governments. The main objectives of the SEZ Act are generation of additional economic activity, promotion of exports of goods and services, promotion of investment from domestic and foreign sources, creation of employment opportunities and development of infrastructure facilities.

66. Various incentives and facilities are offered to both units in SEZs for attracting investments into SEZs (including foreign investment) as well as for SEZ developers. It is expected that these incentives and facilities will trigger a large flow of foreign and domestic investment in SEZs, in infrastructure and productive capacity, leading to the generation of additional economic activity and creation of employment opportunities.

67. The SEZ scheme has generated an enthusiastic response amongst investors, both domestic and foreign, which is evident from the flow of investment and creation of additional employment in the country. In the 63 SEZs notified after 10 February, 2006, investment of the order of Rs. 113.45 billion has already been made in less than one year. These SEZs have so far provided direct employment to 18,457 persons. It is expected that the total investment in these SEZs would be around Rs. 525.61 billion and 15,75,452 additional jobs will be created by December 2009. It is also expected that if all the 234 SEZs, for which formal approvals have been granted so far, become operational, investment of the order of Rs. 3,000 billion may take place and 4 million additional jobs may get created.

IV. REFORMS IN THE TAX SYSTEM

68. Some of the important fiscal measures implemented in the recent past include: rectifying anomalies like inverted tariff structure; rationalising excise duties with a movement towards a median Central Value Added Tax (CENVAT) rate; revisiting the tax exemptions; relying on voluntary tax compliance through taxpayer facilitation; introduction of State-level VAT for achieving a non-cascading, self-enforcing, and harmonized commodity taxation regime; increasing productivity of expenditure through an outcome budget framework, which seeks to translate outlays into better outcomes through monitorable performance indicators; and innovative financing mechanisms like creation of a Special Purpose Vehicle (SPV) for infrastructure projects. While the Central Government has continued to pursue the path of fiscal consolidation as laid down in the FRBM Rules, these efforts have been complemented by the States, which have also initiated a process of fiscal consolidation in line with the Twelfth Finance Commission's (TFC) recommendations.

69. State-level VAT has proved to be an unqualified success. VAT revenues of the implementing States increased by 13.8 percent in 2005-06 and by 24.3 percent in the first nine months of 2006-07.

The next logical step is to phase out Central Sales Tax (CST). The Central Government has reached an agreement with the State Governments to phase out CST. Consequently, the CST rate will be reduced from 4 percent to 3 percent with effect from 1 April 2007.

70. The direct tax reforms include reduction of corporate tax rates and rationalization of income slabs for individuals. The tax base has been continuously broadened by gradually eliminating or capping long-existing exemptions and deductions. The current rates of taxation of personal and corporate income are moderate and at par with international levels. The modernization of tax administration has been a constant endeavour of the Government and electronic filing of returns (compulsory for corporates and optional for others from the financial year 2006-07) reflects the achievements and commitment of the Government on this front. A system of collecting Third Party information on specified high-value financial transactions has been put in place by making it mandatory for certain third parties to file Annual Information Returns about such specified financial transactions. This system has enabled the Government to develop a non-intrusive method of investigation of tax evasion and has promoted voluntary compliance through a higher level of deterrence.

71. The share of direct tax revenue as a percentage of Gross Tax Revenue has increased from 37.6% in 2001-02 to 45.1% in 2005-06. The collection of direct taxes in absolute terms has gone up from Rs. 692 billion in 2001-02 to Rs. 1,652 billion in 2005-06, clocking a growth rate of more than 20% annually over this period.

V. TRADE FACILITATION

72. With a view to reduce the transaction time and cost for the trade, the Directorate General of Foreign Trade (DGFT) has taken a number of initiatives in the recent past, some of which are:

i) All 33 offices of the Directorate have been computerized. Networking of these offices through high speed V-SAT/broad band has been completed.

ii) The website of DGFT, www.dgft.gov.in is both informative and interactive. The website allows online filing of various applications for authorisations.

iii) More than 80% of the applications are received online by DGFT. Processing of these requests is done within 24 hours and necessary permissions are granted on the same day.

iv) Electronic payment gateway for online payment of application fee has been implemented. Efforts are under way to make the operations of DGFT paperless with the introduction of digital signature based operations.

73. The Indian Customs and Central Excise Electronic Commerce/Electronic Data Interchange (EC/EDI) Gateway enables Customs House Agents, Importer, Exporters to file and track customs documents for import and export on 24x7 basis. Persons filing more than 5 documents per working day at any place have also been required to file their documents only through ICE GATE and not through service centres, in order to encourage frequent users of customs services to move over to the electronic filing system. The Department of Revenue has introduced a Risk Management System (RMS) for customs assessment and examination for clearance of imported goods at the Mumbai Air Cargo station, Mumbai Port and Nhava Sheva Port, Chennai Port and Air Cargo station, Delhi Air Cargo station and at a few other major customs stations. This has the following features: (i) System based assessment of risks, (ii) "No assessment, no examination" facility to clients with a proven track record, (iii) Intervention by exception. The introduction of RMS has led to considerable reduction in

the dwell time of incoming cargo. The Department has also introduced a system of electronic payment of import duty on pilot basis in Delhi for the quick clearance of goods.

VI. STRENGTHENING SECTORAL MARKETS

74. The leitmotif of sectoral reforms and policy changes is to supply the institutional capital needed to make markets more competitive and robust. The Government believes in the efficacy of increased competition for delivering desirable social outcomes and has continuously strived to unleash competitive impulses in different economic sectors. The Government is committed to judiciously introducing elements of competition into the markets as the following discussion on several sectors illustrates.

(a) Petroleum and Natural Gas

75. In 1991, a systematic effort on a regular basis to attract private investment for exploration and production, along with the efforts of National Oil Companies (NOC) was initiated. Subsequently the **New Exploration Licensing Policy (NELP)** was approved by the government in 1997 and made operational in January, 1999. NELP provides a level playing field to the private operators by giving them the same fiscal and contractual terms as applicable to NOCs for the offered acreages. Under NELP, production sharing contracts (PSC) for 110 blocks have been signed. In the first five rounds of NELP, the expected investment is of the order of US$ 5 billion. The sixth round of New Exploration Licensing Policy (NELP-VI) was launched on 23 February 2006. In NELP-VI, 55 exploration Blocks (24 deepwater, 6 shallow water and 25 on land) were on offer, covering an area of 3,52,191 Sq. km. out of which bids were received for 52 blocks. The decision on successful bids was taken on 8 February 2007 and the production sharing contracts are expected to be signed shortly.

76. Several other measures have been taken to deepen competition. Since 10 February 2006 restrictions on FDI in the sector have been eased. The Administered Price Mechanism (APM) for the petroleum sector was dismantled on 1 April 2002. Simultaneously, as specified in the Resolution of 2002, private companies have been allowed to participate in the distribution of petroleum products if they invest, or propose to invest, Rs. 20 billion in identified activities in the petroleum sector.

77. A Petroleum and Natural Gas Regulatory Board Act came into effect on 3 April 2006, which envisages the setting up of a Petroleum & Natural Gas Regulatory Board (PNGRB). The Board shall regulate refining, processing, storage, transportation, distribution, marketing and sale of petroleum, petroleum products and natural gas, so as to protect the interest of consumers and entities engaged in specified activities relating to these products and ensure their uninterrupted and adequate supply. Action for setting up the Board is in progress.

78. A policy for the development of natural gas pipelines and city or local natural gas distribution networks, which *inter alia* seeks to promote competition and arms-length business, was notified on 20 December 2006. This policy provides the framework for regulation by the PNGRB, which is expected to become functional shortly. For the upstream (exploration and production) sector, the Director-General of Hydrocarbons was delegated certain powers vested in the Government in September, 2006 to effectively oversee ever increasing exploration and production activities in India for oil, gas, and coal-bed methane.

79. Under the export-import policy, import of crude oil under EXIM Code 27090000 is unrestricted. The data on import shows that non-refining companies are also importing some quantity of crude oil.

80. Several thrust areas for the future have been identified in the Petroleum and Natural Gas sector. These include increase in production, improving pipeline connectivity, encouraging the laying of gas transportation infrastructure and unification of state taxes and removal of tax anomalies.

(b) Textiles

81. India has initiated a series of measures in the past few years to restructure the textiles and clothing industry to prepare it for a quota-free regime. The textiles and clothing sector is labour-intensive and is the second largest employer in India (after agriculture). As a part of the overall policy of de-regulation and de-control, the Government of India has de-reserved garments, hosiery and knitwear from the Small Scale Industries sector. Foreign Direct Investment upto 100% has been allowed in the textiles and clothing sector under the automatic route.

82. The Government of India has been pursuing a path of economic liberalization and structural reforms with a view to integrate its textile industry with the global economy. As a part of the liberalization and reform programme:

- India has removed quantitative restrictions on imports on all textile products, save for a small list of 10 tariff lines at the 8-digit level on account of safety and health exceptions.

- There has been a progressive reduction in the applied Indian tariffs over the years. The peak rates have been slashed from 75% *ad valorem* in 1998 to 30% in 2002 and further to 10% in 2007.

- The export restrictions on raw cotton, cotton waste, and cotton yarn, have been done away with so as to allow free inter-play of market forces. There are no restrictions on the export of textile products.

83. The abolition of the quota regime coupled with the Government's initiatives aimed at restructuring of fiscal duties have led to an improved investment climate in the textile sector. The investments in the textile sector during the 5 year period between 1999-04 were US$ 5 billion. In the next two years, it crossed US$ 6.5 billion. The industry is aiming at investments of the order of US$ 31 billion by 2010. Textile and clothing exports have recorded a growth of 22% in the first year of the quota free regime i.e. 2005-06.

84. The textile industry is poised for strong growth on account of rising domestic consumption, retail credit facilities and the recognition of India as a reliable supplier in many countries of the world. This makes the sector an attractive investment destination.

(c) Steel

85. The Indian steel industry is currently going through an expansion phase backed by a liberalized policy environment. Prospects of domestic demand appear to be excellent, driven by a high investment rate, accelerated growth in the manufacturing industry, and an expansion in physical infrastructure creation.

86. Production of (non-alloy) finished steel recorded an average annual growth of 9.8% from 30.64 MT in 2001-02 to 44.544 MT in 2005-06. In addition, India produced about 2-2.5 MT of Special and Alloy Steel in the last four years. This sector also grew at an impressive rate of around 12% in the corresponding period.

87. India is currently the 7th largest producer of steel in the world with a capability of producing a wide array of steel products. India has also developed upstream capabilities in processed feed-material for the iron and steel industry e.g., Sponge Iron, Pig Iron, Ferro-alloys, Refractory. It is now the largest producer of Sponge Iron in the world and this sector reported a production of 12.649 MT in 2005-06. Production of merchant Pig Iron in India was 4.695 MT in 2005-06.

88. The tariffs on various steel products, which were between 25% to 30% during 2002-03, have been significantly reduced to around 5%. In the span of a single year i.e. 2003-04, the import tariff on most steel products was reduced from 15% to 5% to provide domestic consumers access to global supplies. Consequently, in the following three years, imports of saleable (finished plus semi-finished) steel more than doubled from 1.7 MT in 2003-04 to 4.1 MT in 2005-06.

89. The progressive reduction in import tariffs in recent years has led to domestic prices moving in close correspondence with international prices. The differences between the two sets of prices are largely determined by the external value of the Rupee and import duty rates.

90. The Indian steel industry has turned around during the last four years. The return on capital employed has improved significantly for both public and private sector firms. Presently, the Indian steel industry is capable and credit-worthy enough to fund future projects of capacity expansion through its internal resources and capital raised from the markets.

91. The formulation of the National Steel Policy 2005 (NSP) has been an important development in the progress of the industry. Recognizing the potential for the growth of steel consumption in the country as well as the abundance of raw materials, technology and manpower competence available in the country, the NSP strives to provide an enabling policy environment for the industry to build upon its inherent advantages and to utilise the emerging opportunities. The NSP has set a target of achieving a production level of 110 MT by 2019-2020. The long-term aim of the NSP is that India should have a modern and efficient industry of world standard – in terms of cost, quality and efficiency parameters.

92. The NSP proposes a multi-pronged strategy to move towards the long-term policy objective. On the demand side, the strategy would be to create incremental demand through efforts to promote the use of steel, creation of awareness regarding application of steel and strengthening the delivery chain, especially in the rural areas. On the supply side, the strategy consists of facilitating the creation of additional capacity, removal of procedural and policy bottlenecks in the availability of inputs such as iron ore and coal, supporting higher investments in R&D and human resource development and encouraging the creation of infrastructure such as roads, railways and ports.

93. The ongoing process of global re-location and on-going restructuring of the industry has clearly shown that the focus of the world steel industry is moving towards Asia and especially to countries with an advantageous raw material base combined with large markets with substantial growth potential and technological manpower base. In a deregulated policy environment, much of the stimulus to growth will come from the market forces. However, the Government will have to provide necessary policy support to the sector especially in areas where the market forces do not play out fully or where there are market imperfections.

(d) Information Technology

94. The Information Technology (IT) sector has been one of the fastest growing sectors in the economy. The IT sector comprises IT Software development and IT services, including IT enabled Services (ITES) and Business Process Outsourcing (BPO) and electronics and IT hardware

manufacturing. IT Software development and IT services account for more than 60% of this sector's total revenue.

95. The Government's policy in the IT sector is to promote competition and act as a facilitator for sound growth. In line with this policy objective, the Government has autonomously permitted 100% FDI under the automatic route in IT software and IT enabled services. Likewise, 100% FDI is permitted in the area of electronics and IT hardware manufacturing.

96. With a view to facilitate the growth of the IT sector, two export oriented schemes viz. the Software Technology Parks of India (STPs) and the Electronics Hardware Technology Parks of India (EHTPs) Schemes for promoting the export of IT software and services and electronics and IT hardware products respectively have been in operation since 1991. The units operating under these schemes are exempted *inter alia* from payment of tariff on imports and excise duty on domestic procurement. Both these schemes are implemented by the Software Technology Parks of India (STPI), which is a not-for-profit autonomous organisation under the administrative control of the Department of Information Technology. STPI has 47 centres spread all over the country, through which it extends various services like providing basic infrastructure, including international data communication, access to global Internet and incubation facilities for start-ups and small businesses, statutory services, handholding services and other support services.

97. Since India is a member of the Information Technology Agreement (ITA), tariffs on all the 217 tariff lines have been eliminated from March 2005 to make the Information and Communication Technology (ICT) infrastructure affordable.

98. The Indian IT software and services sector has grown at an annual rate of 28% during the last five years and its contribution to the GDP has increased from 1.2% in 1999-2000 to 4.8% in 2005-06. India is servicing 65% of the global outsourcing market for IT software and ITES and 46% for the global BPO outsourcing market.

99. The Government is trying to ensure that the IT sector does not face a shortage of quality manpower with knowledge and expertise in different domains required by the industry. Accordingly, in addition to initiatives and reforms to improve the overall academic and professional education system by the concerned agencies of the government, measures have also been taken to generate manpower in key verticals like bioinformatics, VLSI design and information security etc. The National Association of Software and Service Companies (NASSCOM) has come up with an assessment of competence programme in order the help the ITES-BPO segment of the business.

100. With a view to further improve the infrastructure facilities for the IT sector, the government has identified a need to set up integrated townships with a special focus on the ITES-BPO industry, in the Tier-II cities of the country, as one of the priority areas. These integrated townships are expected to address the issues of making available world-class infrastructure, including IT facilities, communications, power, roads, airports and other necessary social infrastructure at one location.

101. In order to provide legal recognition for transactions carried out by means of electronic data interchange and other means of electronic communication, commonly referred to as "electronic commerce", the IT Act 2000 had been enacted by the Government.

(e) Telecommunications

102. The Indian telecommunications network, with 190 million connections, is the third largest in the world and the second largest among the emerging economies of Asia. Currently, it is the fastest growing market in the world. The sector, which was growing in the range of 20 to 25 per cent up to

2002-03, has moved to a higher growth path with an average rate of 40-45 per cent during the last two years.

103. The Government has taken several initiatives for the growth of the sector, some of which are:

- All telecom services have been opened to international competition.

- Foreign Direct Investment (FDI) in Basic and Cellular, Unified Access Services, National/ International Long Distance, V-Sat, Public Mobile Radio Trunk Services (PMRTS), Global Mobile Personal Communications Services (GMPCS) and other value added telecom services has been permitted up to 74% (including FDI, FII, NRI, Foreign Currency Convertible Bonds (FCCBs), ADRs, GDRs, convertible preference shares, and proportionate foreign equity in Indian promoters/ Investing Company).

- FDI in Manufacturing of Telecom Equipment has been permitted up to 100% under the automatic route.

- International Long Distance Services (ILDS) have been opened to competition with effect from April 2002.

- The license fee for Infrastructure Providers-II was reduced from 15% to 6% of the Adjusted Gross Revenue in June 2004.

- The entry fee for NLD licenses was reduced to Rs. 25 million from Rs. 1 billion. The entry fee for ILD was reduced from Rs. 250 million to Rs. 25 million.

- Lease line charges have been reduced to make bandwidth available at competitive prices to facilitate growth in IT enabled services.

- One India plan, i.e. a single tariff of Re. 1 per minute for a call under certain schemes to any location in India, was introduced from 1 March 2006 by the public sector companies. This tariff was emulated by most of the private service providers also. This scheme has led to the rapid shrinking of distance in telecommunication and is going to lead to greater benefits for the general consumers as well as trade.

- The annual license fee for National Long Distance (NLD), International Long Distance (ILD), Infrastructure Provider-II, VSAT commercial and Internet Service Provider (ISP) with internet telephony (restricted) licenses was reduced to 6% of Adjusted Gross Revenue (AGR) with effect from January 2006.

- The Government's policy is neutral on the use of technology by telecom service providers subject to availability of scarce resources such as spectrum etc.

- Tariffs for telecommunication services have evolved from a regime where tariffs were determined by the Telecom Regulatory Authority of India (TRAI) to a regime where tariffs are largely under forbearance. TRAI intervenes by regulating the tariffs for only such services, whose markets are not yet competitive.

104. National Long Distance: There is now no limit on the number of service providers in this sector. At present 16 NLD (14 Private and 2 Public Sector) service providers are operating. A licence for National Long Distance service is issued for a period of 20 years, extendable by 10 years at one time.

105. International Long Distance: In the field of international telephony, India had agreed under the GATS to review its opening up in 2004. However, open competition in this sector had been allowed with effect from April 2002 itself. There is now no limit on the number of service providers in this sector. The licence for an ILD service provider is issued initially for a period of 20 years, with an automatic extension of the licence by a period of 5 years. At present 10 ILD service providers (9 Private and 1 Public Sector) are present in the field.

106. Unified Access Services: The Unified Access License Regime was introduced in November 2003. Unified Access Services operators are free to provide, within their area of operation, services which cover collection, carriage, transmission and delivery of voice and/or non-voice messages over the licensee's network by deploying circuit and/or packet switched equipment. The country is divided into 23 Service Areas consisting of 19 Telecom Circles and 4 Metro Service Areas for providing UAS. The licence for UAS is issued on non-exclusive basis, for a period of 20 years, extendable by 10 years at one time within the territorial jurisdiction of a licensed Service Area. At present 3 to 6 service providers (2-5 private and 1 public sector) are present in most of the service areas.

107. Internet and Internet Telephony Service Providers: Internet services were opened to the private sector in November 1998 without internet telephony. The token licence fee is Re. 1 for Internet Services. Internet with Telephony (computer to computer, SIP to SIP and computer to out side India) was opened to the private sector in April 2002. The licence fee is 6% of AGR for Internet Telephony. There are 385 internet service providers and 125 internet telephony service providers at present.

108. With the opening of the telecom sector to private operators, their share in the number of subscribers has been increasing rapidly. The share of the private sector in the number of telephones has increased from 15.12% (6.80 million telephones) in March 2002 to 65.0% (123.44 million telephones) in December 2006.

(f) Financial Sector

(i) Reforms in the Foreign Direct Investment (FDI) Regime

109. India has been opening up its external sector steadily and several new measures have been taken since 2002. The foreign exchange regime of India is now considered to be one of the most liberal amongst countries where restrictions on the capital account still exist. The FDI policy has been to encourage investment in manufacturing, services and infrastructure. Foreign investment is permitted up to 100 per cent of the paid up capital in most sectors, including in Non Banking Finance Companies (NBFCs) under the automatic route. FDI is also permitted up to 49%, with prior government approval, in Asset Reconstruction Companies registered with the Reserve Bank of India (RBI).

110. As per current policy, FDI up to 100% is allowed under the automatic route in most sectors/activities of manufacturing. FDI under the automatic route does not require the prior approval of either the Government of India or the RBI. Investors are only required to notify the concerned Regional office of the RBI within 30 days of the receipt of inward remittances and file the required documents with that office within 30 days of the issue of shares to foreign investors.

111. Foreign investments in equity capital of an Indian company under the Portfolio Investment Scheme are governed by the regulations of the RBI/Securities & Exchange Board of India (SEBI).

Rationalisation of the FDI Policy

112. A major liberalization of the FDI Policy was carried out in February 2006 which, *inter alia*, allows FDI under the automatic route in sectors such as potable alcohol, hazardous chemicals, industrial explosives, greenfield airport projects etc.; enhances FDI caps to 100% for setting up infrastructure relating to marketing in the Petroleum & Natural Gas sector and permits FDI up to 100% under the automatic route for power trading, subject to compliance with regulations under the Electricity Act, 2003

113. By and large, the FDI policy followed by India has encouraged more inflows into the country. Inflows of foreign direct investment (FDI) into India have witnessed a susbstantial growth during the financial year 2006-07 and are expected to be more than double the inflows recorded in the previous year. FDI equity inflows in the period, April-December 2006, have been US$ 9.3 billion – the highest ever received in equity capital since the commencement of economic liberalization in India. According to the World Investment Report 2006 published by UNCTAD, FDI stocks as a percentage of GDP have grown from a level of 0.5 in 1990 to 5.8 in 2005.

(ii) Reforms in the Foreign Exchange Market

114. Several steps have also been taken to liberalise foreign exchange transactions. A key consideration has been the rationalisation and simplification of procedures with a view to facilitating prompt and efficient customer service in external transactions. Foreign institutional investors (FIIs) registered with the SEBI are allowed to invest in the Indian market, including in debt securities, subject to certain limits. The limits for FII investment in government securities and corporate debt have been gradually enhanced in order to provide more investment opportunities to FIIs and greater depth to the Indian debt market. Certain qualified Mutual Funds are also permitted to invest in overseas exchange traded funds. In February 2004, a Liberalised Remittance Scheme was introduced whereby resident Indians were permitted to remit up to US$ 25,000 per calendar year, for any current or capital account transaction or a combination of both.

115. The RBI, in consultation with the Government of India, had appointed a Committee on Fuller Capital Account Convertibility (FCAC) (S.S. Tarapore, Chairman) on 20 March 2006. The Committee submitted its report to the RBI in July, 2006 which has been placed on the website of the RBI. Following the recommendations of the Committee, several measures have been announced in October 2006 (Mid-term Review of Annual Policy Statement for the Year 2006-07) for further liberalising foreign exchange transactions. The policy announcements relate to *inter alia* liberalisation of Exchange Earners' Foreign Currency (EEFC) accounts , increased access to External Commercial Borrowings (ECBs), enhancement of ceiling of overseas investment by mutual funds, bank guarantee/letter of credit to cover temporary trade related credits and remittances out of Non-resident Ordinary (NRO) accounts.

(iii) Deregulation of Interest Rates

116. Progressive deregulation of financial markets in recent years has improved the competitive environment in the financial system and strengthened the transmission mechanism of monetary policy. The interest rates have been largely deregulated except for (i) savings deposit accounts, (ii) non-resident Indian (NRI) deposits, (iii) small loans up to Rs. 200,000 and (iv) export credit. A short term credit to farmers up to Rs. 300,000 at 7 per cent per annum has been made available from *kharif* 2006-07 in order to help farmers obtain credit at a reasonable rate.

117. The Bank Rate, which was reduced from 6.5 per cent to 6.25 per cent with effect from October 30, 2002 and further to 6 per cent with effect from 30 April 2003, has remained unchanged at

6 per cent. The cash reserve ratio (CRR) was reduced to 4.50 per cent with effect from 14 June 2003 from 4.75 per cent. Thereafter, the CRR was increased to 5.0 per cent in two stages of 25 basis points each with effect from 18 September 2004 and 2 October 2004 to combat inflationary pressures. On 8 December 2006 it was announced that the CRR rate would be hiked by one-half of one percentage point on net demand and time liabilities (NDTL) in two stages effective from 23 December 2006 (5.25 percent) and 6 January, 2007 (5.50 percent). The RBI announced on 13 February 2007 a further hike in CRR by 25 basis points each effective from the fortnights beginning 17 February and 3 March 2007. The statutory liquidity ratio (SLR), which was 37.75 per cent in 1992-93, has been brought down to 25 per cent with effect from 25 October 1997. Currently, the stipulated level of SLR remains at 25 per cent.

118. On the deposit side, banks have been given the freedom to offer fixed rate or floating rate loans with a reset at six-monthly intervals, linked to an anchor rate. The lending rates have been gradually deregulated since 18 October, 1994. The lending rates currently regulated by the RBI are the ceiling rates for export credit and small borrowers up to Rs. 200,000. In order to enhance transparency in the pricing of loan products, banks have been advised to fix their Benchmark Prime Lending Rate (BPLR) after taking into account: (i) actual cost of funds (ii) operating expenses and (iii) a minimum margin to cover provisioning/capital charge and profit margin and ensure that the BPLR truly reflects the actual cost.

(iv) Banking Sector Reforms

119. The financial sector reforms initiated in India are in harmony with reforms in other sectors of the economy and are a component of the overall scheme of structural reforms. The objectives of reforms in the banking sector were to strengthen Indian banks, make them internationally competitive, and encourage them to play an effective role in accelerating the pace of growth.

120. Banking sector reforms in India are based on five fundamentals, viz. strengthening of prudential norms and market discipline, adoption of appropriate international benchmarks, management of organisational change and consolidation, technological up-gradation, and human resource development. A hallmark of the entire financial sector reform process has been the element of phasing, with due consideration of the timing, pace and sequencing, following extensive consultations with the stakeholders at each stage. Deregulation, technological up-gradation, and increased market integration, have been the key factors driving change in the financial sector. The steady and sustained reform measures taken over the last four years have transformed the banking sector in India into a reasonably strong, diverse and resilient system. The major initiatives undertaken relate to deregulation, prudential measures and approach to supervision, competition and enabling measures.

Deregulation

121. Two major problems confronted by the banking system in the pre-reform stage were large-scale pre-emption of banks' resources by way of statutory reserve requirements and administered interest rates. These significantly impacted their ability to deploy their funds as well as price them. Removal of these constraints required a planned reduction in the statutory reserve requirements along with a gradual deregulation of interest rate prescriptions. The statutory preemptions in the form of SLR and CRR have been brought down in a phased manner. The recent amendment to Section 42 of the RBI Act, 1934, in June 2006 vests the RBI with the power to prescribe the CRR for scheduled banks without any floor or ceiling rate.

Prudential measures and supervision

122. Prudential norms on capital adequacy, income recognition, asset classification, provisioning relating to advances and investment, have been introduced. These are periodically reviewed and refined to meet international standards. With the gradual liberalisation of the Indian financial system and growing integration of the domestic market with the external markets, the risks associated with banks' operations have become increasingly complex, requiring strategic management. The RBI has issued guidelines on Asset-Liability Management (ALM) systems and on integrated risk management systems in banks. Due to the diversity and varying sizes of their balance sheets, banks have been advised to design their risk management architecture taking into consideration their size, complexity of business, risk philosophy, market perception and level of capital. With a view to fine-tuning risk management systems in banks and to help smaller banks in achieving the minimum standards, the Reserve Bank had issued guidance notes on credit risk and market risk in 2002. Recently, guidance notes on operational risk and guidelines on managing risks in outsourcing of financial services by banks as well as guidelines regarding capital charge on market risk have also been issued.

123. In view of the increased focus on empowering supervisors for undertaking consolidated supervision of bank groups, effective from March 2003, preparation of consolidated financial statements (CFS) have been mandated for all groups where the controlling entity is a bank. In recent years, prevention of money laundering has assumed importance in international financial relationships. In this context, the Reserve Bank has revised and tightened the guidelines on 'Know Your Customer' (KYC) principles in November 2004 in line with the recommendations made by the Financial Action Task Force (FATF) on standards for Anti-Money Laundering (AML) and Combating Financing of Terrorism (CFT).

124. The twin pillars of supervision, viz., on-site examination and off-site monitoring and surveillance have been evolving dynamically in response to developments in the Indian financial system and international best practices. The on-site examination of banks is modeled on the CAMELS (Capital, Asset quality, Management, Earnings, Liquidity and Systems) framework. The Off-site Monitoring and Surveillance (OSMOS) system consists of a set of structured returns designed to capture critical information concerning the financial health of supervised entities at frequent intervals. It enables the Reserve Bank to carry out continuous supervision and set priorities for the allocation of scarce supervisory resources.

Competition

125. As a part of the reforms programme, initially there had been infusion of capital by the government in public sector banks, which was followed by expansion of the capital base with equity participation by private investors up to 49 per cent. Guidelines have since been laid down in respect of the establishment of new banks in the private sector and foreign banks have been allowed more liberal entry. Post-reform, 11 new private sector banks are in existence. As a major step towards enhancing competition in the banking sector, foreign direct investment is now allowed up to 74 per cent from all sources in private sector banks under the automatic route, subject to conformity with the guidelines issued from time to time. Foreign banks are allowed to have a banking presence in India either through the establishment of subsidiaries incorporated in India or through branches.

Enabling measures

Institutional and legal reforms

126. A high powered Board for Financial Supervision (BFS) had been constituted in 1994, with the mandate to exercise powers of supervision and inspection in relation to banking companies, financial

institutions and non-banking companies. A Board for Regulation and Supervision of Payment and Settlement Systems (BPSS) has been constituted to frame policies relating to the regulation and supervision of all types of payment and settlement systems, set standards for existing and future systems, authorise the payment and settlement systems and determine criteria for membership to these systems. The government has enacted 'The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002,' which provides, *inter alia*, for the enforcement of security interest for realisation of dues without the intervention of courts or tribunals. An independent Banking Codes and Standards Board of India (BCSBI) on the UK model has also been set up, to ensure that a comprehensive code of conduct for fair treatment of customers is established.

Transparency and disclosure

127. Transparency and disclosure standards as per international best practices are being implemented in a phased manner. The initial disclosure requirements relate to capital adequacy, NPAs, profitability ratios and details of provisions and contingencies. Disclosure requirements have been further broad-based and banks have been advised to disclose the maturity pattern of deposits, borrowings, investments and advances and foreign currency assets and liabilities, movements in NPAs, provisions and contingencies, penalties imposed, exposure in derivatives and lending to sensitive sectors.

Consultative process

128. In order to ensure timely and effective implementation, the Reserve Bank has been adopting a consultative approach before introducing policy measures. On all important issues, working group reports or technical reports are prepared, generally encompassing a review of international best practices, options and the way forward. Draft reports are often placed in the public domain and the final report takes due account of all inputs, in particular, from the industry associations and self-regulatory organizations.

Dissemination of Credit Information

129. In order to establish an efficient credit information system that would help in enhancing the quality of credit decisions and improving the asset quality of banks, the Reserve Bank had facilitated the establishment of the Credit Information Bureau India Ltd. (CIBIL). With a view to strengthening the legal mechanism and facilitating credit information bureaus to collect, process and share credit information on borrowers of banks/FIs, the Government of India had passed and notified 'The Credit Information Companies (Regulation) Act, 2005, covering registration, responsibilities of the bureaus, rights and obligations of the credit institutions and safeguarding of privacy rights.

Implementation of Basel II

130. Foreign banks operating in India and Indian banks having a presence outside India will start implementing Basel II with effect from 31 March, 2008. All other scheduled commercial banks would be required to implement Basel II with effect from 31 March 2009.

The Impact of Reforms

131. Financial sector reforms have had a significant impact on the overall efficiency and stability of the banking system. The average capital to risk-weighted assets ratio (CRAR) of all scheduled commercial banks increased from 9.2 per cent as on 31 March, 1994 to 12.3 per cent as on 31 March 2006. The gross NPAs as a proportion of gross advances of the banking system have declined steadily and appreciably over the years from 14.4 per cent at end-March 1998 to 3.3 per cent

at end-March 2006. Over the same period, the percentage of net NPAs to net advances declined from 7.3 per cent to 1.2 per cent. The absolute level of the gross NPAs has also decreased in the recent past. The profitability of banks has also improved during the period. The return on assets (RoA) of all banks rose from 0.4 per cent in the year 1991-92 to 0.9 per cent in 2005-06. The net interest income as percentage to total assets (the spread) declined from 3.3 in 1991-92 to 2.8 in 2005-06. The business per employee of PSBs has increased from Rs. 18.8 million in 2002 to Rs. 31.15 million in 2005.

(v) Insurance Sector

132. There are 16 life insurers, 15 non-life insurers and 1 reinsurer operating in the country. Of these, there are 15 private life insurers and 9 non-life private insurers. The first year premium of the life insurance industry has grown at the rate of 30% per annum to Rs.388 billion for the year ending 31st March, 2006 as compared to Rs.97 billion in 2000-01. Like-wise the non-life insurance industry also witnessed an annual average growth of 15.72% by writing gross premium of Rs. 204 billion in 2005-06 up from Rs. 98 billion in 2000-01. Insurance premium per capita in India has increased to US$22.70.

133. One of the significant policy changes envisaged by the government is a comprehensive amendment to the Insurance Act. The major thrust is on modernizing the Act based on the new developments in the insurance sector and in removing the redundancies of the erstwhile era. Some of the major suggestions include modification of the FDI ceiling in Indian insurance companies; change in the procedures for licensing of agents; providing flexibility in the role of Insurance Councils; consolidation of the investment provisions for both life and general Insurers and to give flexibility to the Authority to determine the types of investment, the method and manner of Investments under the Regulations.

134. The other important policy change being considered by the Government of India is a reduction in the capital requirements for a stand-alone health insurance company. The IRDA is in the process of framing a separate set of regulations in the health insurance sector. In case of new health products being filed with the IRDA, the pre-existing disease clause has been standardized. ICD-10 coding has been made mandatory for insurance companies and third party administrators (TPAs).

135. One of the significant events in the insurance sector is the detariffication of the general insurance industry from 1 January 2007. Insurance companies have now been given the freedom to vary their premium rates. However, the terms and conditions of the insurance policies have not been allowed to be changed till 31 March 2008. The freeing of the terms and conditions as well as the premium rates of tariff policies simultaneously could have resulted in instability and upheaval which would not have been in the interests of the policyholders as well as the industry. Therefore, freeing of only the premium rates was carried out so that the movement to a tariff free regime is in an orderly, gradual and planned manner.

(vi) Capital Market Reforms

136. Major reforms in the primary market since 2002 include introduction of green shoe option; flexibility in price band indication in book building issues; proportionate allotment to Qualified Institutional Buyers (QIBs) in allotment of shares in public issues; introduction of 10% margin for QIB bids in public issues; rationalization of disclosure requirements; ECS facility for public issue refunds; facility of shelf prospectus for public sector banks and public financial institutions; increased allocation of shares to retail investors; and introduction of guidelines for delisting of securities.

137. Major reforms in the secondary market since 2002 include shift to rolling settlements on T+2 basis; implementation of straight through processing for all institutional trades on stock exchange; introduction of margin trading; introduction of single stock futures and options trading in addition to index derivatives. The National Stock Exchange (NSE) is now the leading exchange in the world in single stock derivatives trading. In 2004, the Securities Law (Amendment) Act 2004 was enacted, to enable all stock exchanges to be corporatized and demutualized in accordance with a scheme approved by SEBI.

VII. CORPORATE GOVERNANCE

138. Norms for corporate governance, which include details about the composition of the board of directors, board procedures, code of conduct of board members and composition and powers of an independent audit committee are specified in the listing agreement of companies listed on stock exchanges. From January 2006, all listed companies are required to adopt these corporate governance requirements. All new listing in particular would need to ensure compliance with corporate governance provisions and make disclosures to this effect in the offer document for their IPOs. Companies are required to file a quarterly compliance report with the stock exchanges.

139. In order to provide a comprehensive legal framework to address the anti-competitive practices of enterprises, the Government has enacted the Competition Act, 2002. However, implementation of the core enforcement provisions of the Act has been delayed because of legal challenges to certain provisions of the Act. These are being addressed through the Competition (Amendment) Bill, 2006, which is expected to be enacted soon by Parliament.

VIII. INDIA AND THE WTO

(a) Intellectual Property Rights

140. India amended its legislations relating to the protection of intellectual property rights in order to honour all its commitment under the TRIPS Agreement. These changes were reflected in the last Trade Policy Review. During the current policy review period, further amendments have been made in 2005 to the Patents Act, 1970. Indian patent law is now fully compatible with the TRIPS Agreement.

141. With the amendments made in 2005, both process and product patent protection is now available in all fields of technology, including food, pharmaceuticals and chemicals. The law now has provision both for pre-grant and post-grant opposition in the Patent Office. The term of patent protection is now 20 years for all inventions.

142. A provision has also been introduced in the Patents Act, in 2005, to enable the grant of compulsory licenses for export of medicines to countries with limited or no manufacturing capacities to meet emergent public health situations in accordance with Decision of the WTO of 30 August 2003 on the Implementation of Paragraph 6 of the Doha Declaration on the TRIPS Agreement and Public Health. India has also accepted the protocol amending the TRIPS Agreement (Article 31*bis*) which incorporated the flexibilities agreed to in the Doha Ministerial Declaration.. The Patent law now effectively balances and calibrates intellectual property protection with public health concerns and national security.

143. The period 2002-06 witnessed a rise in the registration and granting of various forms of intellectual property rights. During 2001-02, the number of patent applications filed were 10,592, and 1,591 patents were granted. In 2005-06, the numbers went up to 24,505 and 4,320, respectively; reflecting an increase of 130 percent in four years in the number of patent applications, and an

increase of 170 percent in the number of patents granted. A similar increase has been noticed in the case of other intellectual property rights also. While trademark registrations have gone up from 6,204 in 2001-02 to 184,325 in 2005-06; industrial design registrations have increased from 2,426 to 4,175 during the same period.

144. Such an increase in the number of patents and other intellectual property rights is indicative of an economic and institutional regime which provides incentives for the efficient use of existing and new knowledge and for exhibiting entrepreneurship.

145. Provisions exist in the various laws for dealing with counterfeiters and those who engage in the manufacture and marketing of pirated goods. Persons found guilty of indulging in the manufacture of pirated products or in any way dealing with pirated/spurious goods are tried under the relevant legislations governing the offences. Further, the Court may also order that the goods which are found to be infringing and materials and implements, the predominant use of which is made in the creation of infringing goods shall be seized, forfeited or destroyed.

146. The Customs Act empowers the Central Government to prohibit or restrict import or export of goods in order to protect trademarks, copyrights and patents. The Central Government has also issued a notification prohibiting import of goods in violation of the Trade Marks Act.

147. Courts in India have also issued on occasion an 'Anton Pillar Order' which originates from British Law and which in substance provides for *ex-parte* seizure of infringing goods in cases where incriminating materials are likely to be tampered with and such relief could facilitate preservation of evidence at the trial stage.

148. The actual enforcement of the law is the concern of the State Governments through the use of its enforcement machinery. Most of the States have set up Intellectual Property Rights Cells to look into the complaints of violation and infringement of Intellectual Property Rights. The primary responsibility for investigating complaints of manufacture of pirated goods rests with the concerned State police within whose jurisdiction the manufacturing unit is situated. The State police takes action in accordance with the rules provided under the different Acts relating to the counterfeiting of goods and initiates proceedings against the guilty. The Central Government has set up an Inter-Ministerial Coordination Committee on Intellectual Property Rights Enforcement Issues to have a focused approach in the matter..

(b) Services

149. The expected contribution of Services to the GDP is about 55.1% in 2006-07. The sector accounted for about 37% of the country's exports in the combined basket of goods and services. These statistics reveal in unambiguous terms the importance of the sector for India.

150. The services' negotiations of the Doha Development Agenda (DDA) are significant for both developed and developing countries. These negotiations intend to secure a pro-development outcome for developing countries and at the same time to strengthen the international trading system making it more open and based on fair and equitable rules and disciplines.

151. As a part of these negotiations, India had submitted its Initial Offer in January 2004 and Revised Offer on 24 August 2005, which marked a substantial improvement over its Initial Offer. The new areas covered in the Revised offer include architectural, integrated engineering and urban planning and landscape services; veterinary services; environmental services; distribution services; educational services; recreational, cultural and sporting services, maintenance and repair of aircraft. Further, the coverage and commitments were improved in construction and related engineering

services; tourism services; financial Services etc. New commitments have also been offered in cross border supply in a large range of other business services; professional services; research and development services; rental and leasing services; real-estate services; etc. Thus, in the current round of services negotiations under GATS, India has offered to substantially increase the depth and coverage of its commitments in its Revised Offer.

152. India's interest in the ongoing negotiations lies in seeking from developed countries improved modal commitments in Cross Border Supply of Services (Mode 1) and Movement of Natural Persons (Mode 4). India's Mode 4 objectives are driven by the competence of its service professionals, while its Mode 1 objectives are driven by its strong competitive edge in Information Technology and Information Technology Enabled Services. In Mode 1, India would like to have binding commitments to impart predictability and certainty in the public policy environment of its trading partners. In Mode 4, India wants the removal of the Economic Needs Test (ENT), a clear prescription of the duration of stay, provisions of extension, etc. Such commitments will lead to gains for both developed and developing countries It needs to be noted that an estimate carried out by the WTO with regard to the share of the four modes of supply in the global trade in services shows that while Mode 4 contributes only 1% of all services trade, the shares of Mode 1, Mode 2 and Mode 3 are 28%, 14%, and 57% respectively. The imbalance between the various modes of supply of services needs to be corrected.

153. As noted above, Mode 4 is extremely important for India and without a satisfactory outcome in this area, India would be hard pressed to respond favorably to the requests for market access. Mode 4 commitments are important for India because our service providers continue to face barriers in the markets of developed countries, particularly the US and EC. Some such barriers are:

- Non-recognition of Indian qualifications, training and work experience.

- Burdensome entry procedures, including those relating to Visas.

- Layers of regulations, which are not transparent, making it difficult for a service provider to understand what licensing and qualifications are necessary and how shortfalls, if any can be met.

- Imposing numerical quotas on the number of service providers.

- Imposition of an Economic Needs Test and Labour market tests, making it difficult to access markets.

- Requirement of wage parity, which constricts the ability of developing countries to exploit their comparative advantage in labour.

- Discriminatory treatment of service providers in terms of tax treatment and contribution to social security.

- Residency and Citizenship requirements.

154. The above restrictions can be met by taking the following measures:

- Ensuring market access in a wide range of sectors for Mode 4, particularly professional services, other business services, financial services, telecom services.

- Ensuring full National Treatment commitments in Mode 4.

- Ensuring that the Mutual Recognition Agreements (MRAs) being negotiated at the bilateral level give adequate opportunity for participation of third party Members in line with the obligations under Article VII of GATS.

- Deeper disciplines on domestic regulation under VI:4 of GATS and building on provisions in Article VI:6 ensuring fairness and objectivity in the evaluation of competence and recommendations for remedial action.

- Ensuring implementation of Transparency commitments under Article III of GATS; a one stop website for each profession would be a good start.

- Transparent and efficient processes for the evaluation of qualifications.

- A liberal visa regime that not only ensures that market access commitments taken are met effectively but also ensuring that all regulatory requirements are met.

155. Another area of crucial interest to India in services is the development of disciplines in Domestic Regulation (DR) particularly in qualification and licensing requirements and procedures, without which Mode 4 access is severely impeded. Negotiations on Domestic Regulation are under way at the WTO. India wants that disciplines in DR should be put in place before the end of the current round as per the Hong Kong mandate. India desires to strike a balance between the right to regulate and regulations becoming unnecessary barriers to trade.

156. In pursuance of the Hong Kong Ministerial directives under which plurilateral discussions were initiated at the WTO, India has received plurilateral requests in 14 different service sectors, including Telecom, Finance, Maritime, Environment, Education, Air transport, Energy, Audio Visual and Retail. India is the coordinator of the plurilateral requests on Mode 1 and Mode 4. India is also the co-sponsor of plurilateral requests on Computer and Related Services (CRS) and Architectural, Engineering and Integrated Engineering Services (AIE).

(c) Some Impediments to the Growth of India's International Trade

(i) Unwarranted use of Trade Defense Action

157. India has a current share of only around 1% of global merchandise exports. In 1995, the share was much less. However, it has been subjected to a disproportionate number of trade defense actions. For instance during the period 1 January 1995 to 30 June 2006, Indian products have been subjected to 124 out of the 2938 anti-dumping actions initiated globally, which amounts to more than 4% of the total. These 124 initiations resulted in measures being taken in 69 cases (55.6%). The large scale initiation of anti-dumping action, led to considerable disruption and loss of trade. Again out of the 69 measures, 15 each relate to chemicals and plastics, 8 to textiles and 22 to metal products (mainly iron and steel products)- areas in which India has gained some measure of comparative advantage globally in recent times. The most noteworthy of the anti-dumping cases relate to bedlinen, hot rolled coils and shrimps.

158. It also needs to be mentioned that in many cases, importing countries have initiated both anti-dumping and countervailing action simultaneously, to ensure that their objective is satisfied in one way or the other. In the matter of countervailing measures, 30 out of 41 cases (till 2004), had been initiated by the developed countries.

(ii) Textiles & Clothing

159. Textiles and Clothing is an important sector for India. Currently, the sector contributes about 14 percent to the industrial production of the country. The sector is the second largest provider of employment after agriculture, employing close to 85 million people; 35 million directly in textiles and 50 million in allied activities. It also contributes substantially to India's export earnings, accounting for nearly 17% of the country's total exports.

160. The textiles and clothing sector has witnessed a relatively high incidence of trade defense action. This includes back-to-back anti-dumping action. Some of the restraining countries took frequent recourse to the anti-dumping and countervailing measures in respect of India's textile and clothing products, notwithstanding the fact that their exports were already circumscribed by quota limits. In many cases investigations were subsequently terminated. Nevertheless, damage to trade did occur due to the chilling effect caused by the initiation of such investigations.

161. In the Uruguay Round, the efforts of the developing countries were centered on the more visible and immediate effects of quota restrictions and, therefore, on getting the sector reintegrated into the same rules and disciplines of the multilateral system as for any other sector of industrial goods. Consequently, textiles and clothing tariffs escaped being subjected to any significant reductions and therefore remain much higher than other industrial products.

(iii) SPS and TBT issues

162. The rising incidence of non-tariff barriers, in the form of Sanitary & Phytosanitary (SPS) Measures and Technical Barriers to Trade (TBT), has emerged as a major trade concern. New SPS and TBT-related measures very often have market access implications and it is important that these issues be addressed adequately.

163. The WTO Agreements recognize the diversity of standards across countries, but the issue of actual needs also needs to be factored in. Many times these standards and measures are such that they impose inappropriate or unwarranted economic and social costs on the exporting countries – more so if the exporting countries are the developing and the least developed countries- without actually conferring a commensurate gain to the importing countries. Such measures thus impede trade and deny a trade opportunity to developing countries like India. For instance India had to wait, without much scientific reason, for almost two decades to secure access for its mangoes to two of the leading developed countries.

164. Besides the above, these mandated standards change frequently, and that too quite rapidly, leading to compliance cost implications. As the exporters/producers get ready to meet a particular standard, the major importing countries move to a different standard, which may be only slightly different from the earlier one. But adjusting again to the new standard can involve huge costs for the producers. Sometimes incremental higher standards or regulations entail a higher share in total production costs, making low-value products relatively more vulnerable and often forcing producers out of business.

165. Given the above issues, the WTO members need to embark on a collaborative and cooperative approach for realizing the free trade objective. Only such an approach would lead to trade enhancement, sustainable development and benefits to the national economies in terms of improved resource efficiency. Ex-ante assessment of the impact of these standards and regulations can be an important step in the right direction.

IX. REGIONAL TRADING ARRANGEMENTS

166. India attaches significance to her participation in regional trade agreements within the framework of multilateral rules. India has been instrumental in setting up the South Asian Association for Regional Cooperation (SAARC), whose major achievement in 1995 was the conclusion of the negotiations on trade preferences within the framework of the SAARC Preferential Trading Arrangement (SAPTA). The Agreement on setting up the South Asian Free Trade Area (SAFTA) was signed by member countries of SAARC in January 2004 and a phased tariff liberalization programme under its aegis, has been implemented from 1 July 2006.

167. India has bilateral trade agreements with its two neighbouring LDCs, namely, Bhutan and Nepal which provides them preferential market access. A Free Trade Agreement between India and Sri Lanka was made operational in March, 2000. The Agreement envisages phasing out of tariffs on all products except for a limited number of items in the Negative List. While India has completed the process of tariff elimination in March 2003, Sri Lanka is scheduled to reach zero duty by 2008. The two countries have initiated negotiations in August, 2004 on a Comprehensive Economic Partnership Agreement (CEPA) which covers trade in services and investment. A Preferential Trade Agreement was signed between India and Afghanistan on 6 March 2003 in New Delhi which provides for, among others, establishing a PTA between the two countries to promote harmonious development of economic relations and free movement of goods through reduction of tariffs.

168. The text of the Bangkok Agreement has been re-negotiated and has been re-named as the Asia Pacific Trade Agreement (APTA). This was signed in the first session of the Ministerial Council on 2 November 2005 in Beijing. The APTA is operational among five countries, namely, Bangladesh, PR China, India, the Republic of Korea and Sri Lanka. Till date three Rounds of Trade Negotiations have taken place under APTA. The third Round of tariff concessions have been implemented from 1 September 2006.

169. India is also a member of a regional grouping named BIMST-EC (Bangladesh, India, Myanmar, Sri Lanka, Thailand Economic Cooperation) formed in 1997. During the first BIMST-EC Summit held in July 2004, the initiative has been renamed as the Bay of Bengal Initiative for Multi-sectoral Technical and Economic Cooperation (BIMSTEC) with the admission of Bhutan and Nepal as members to the grouping. The Framework Agreement on the BIMST-EC FTA was signed on 8 February 2004 in Phuket, Thailand. The Framework Agreement includes provisions for negotiations on an FTA in goods, services and investment. A Trade Negotiating Committee (TNC) has been constituted to carry forward the programme of negotiations.

170. An India – Singapore Comprehensive Economic Agreement (CECA) has been signed on 29 June, 2005. The Agreement came into force on 1 August 2005. A Framework Agreement on Comprehensive Economic Cooperation between ASEAN and India and an India – Thailand Framework Agreement have also been signed and an FTA on Goods, Services and Investment are under negotiation under its aegis. Framework Agreements on economic cooperation followed by PTA have also been entered into with MERCOSUR and Chile. India is also engaged with the Gulf Cooperation Council and Mauritius for an FTA/Comprehensive Economic Cooperation Partnership Agreement respectively. Joint Task Forces with the respective countries have also been set up to negotiate a Comprehensive Economic Partnership Agreement with Korea and Japan.

171. Negotiations for a broad based trade and investment agreement with the European Union are expected to commence in May 2007 provided all the requisite approvals are in place.

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