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TOPIC GENERAL STUDIES 3: ECONOMICS- ECONOMIC DEVELOPMENT- GOV POLICIES

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1) SEBI MULLS SRO FOR INVESTMENT ADVISERS

The Securities and Exchange Board of India (SEBI) has proposed a self-regulatory organisation (SRO)for the growing number of investment advisers to address issues related to the quality of advice given to investors by such entities.

Key facts:

• SRO is the first-level regulator that performs the crucial task of regulating intermediaries representing a particular segment of securities market on behalf of the regulator. It would be seen as an extension of the regulatory authority of the SEBI and would perform the tasks delegated to it by the SEBI.

• The role of SRO is developmental, regulatory, related to grievance redressal and dispute resolution as well as taking disciplinary actions.

• The regulator has proposed a governing board with at least 50% public interest directors along with 25% representation each of shareholder directors and elected representatives.

• Further, the governing board can appoint a managing director or chief executive officer to manage the daily affairs of the SRO.

Need:

• SEBI was in receipt of a large number of complaints alleging charging of exorbitant fees, assurance of returns, misconduct etc. by investment advisers. Given the growth in this segment of the market, it was felt that the time is appropriate to initiate the formation of an SRO.

2) ASIAN TEA ALLIANCE

Recently the Asian Tea Alliance (ATA), a union of five tea-growing and consuming countries, was launched in Guizhou, China.

Details

• The forging of this alliance is an outcome of the signing of a memorandum of understanding in December 2018 between the Indian Tea Association and China Tea Marketing Association.

• Participating countries: India, China, Indonesia, Sri Lanka and Japan. o It will work towards enhancing tea trade, promoting tea globally, and creating a sustainability agenda for the future of Asian tea.

Climatic Condition suitable for Tea

• Temperature: 210C to 290C is ideal for Tea. The lowest temperature for the growth of tea is 160C.

• Rainfall: 150-250 cm of rainfall is required for tea cultivation.

• Soil: Tea shrubs require fertile mountain soil mixed with lime and iron. The soil should be rich in humus.

• Land: Tea cultivation needs well drained land. Stagnation of water is not good for tea plants. Indian Tea Industry: At a Glance

• As of 2018 India was the second largest producer of Tea in the world after China.

• India stands fourth in terms of tea exports after Kenya, China and Sri Lanka respectively.

• India is one of the world’s largest consumers of tea, with about three-fourths of the country’s total produce consumed locally.

• The main tea-growing regions are in Northeast India (including Assam) and in north Bengal (Darjeeling district and the Dooars region) along with Nilgiris in south India.

3) DRAFT NATIONAL URBAN POLICY FRAMEWORK

The Ministry of Housing and Urban Affairs released its first draft of the National Urban Policy Framework (NUFP), 2018.

Background

• India has been urbanized at a fast pace in the last two decades, yet despite many efforts, India's cities are struggling to provide for their current population.

o The U.N. World Urbanization Prospects 2018 report states that about 34per cent India's population now lives in urban areas.

o This shows an urgent need to revisit the country's urban strategy.

• Building both on the international frameworks as well as the national missions, the National Urban Policy Framework (NUPF) outlines an integrated and coherent approach towards the future of urban planning in India.

• The NUPF is structured along two lines:

(i) 10 core philosophical principles of urban planning, and

(ii) these principles are then applied to ten functional areas of urban space and management.

• The framework provides recommendations on these functional areas.

10 Urban Sutras (Principles) of NUFP

• Cities are clusters of human capital

• Cities require a 'sense of place

• Not static Master Plans but evolving ecosystems

• Build for density

• Public spaces that encourage social interactions

• Multi-modal public transport backbone

• Environmental sustainability

• Financially self-reliant

• Cities require clear unified leadership

• Cities as engines of regional growth.

4) MUNICIPAL BONDS

The Reserve Bank of India (RBI) has allowed foreign portfolio investors (FPIs) to invest in municipal bonds.

What are municipal bonds?

• They are debt securities issued by government or semi-government institutions who need funding for civic projects.

• Normally, they are issued and redeemed at par and carry a fixed interest rate.

• There are two types of municipal bonds o General obligation bonds are issued for enhancing civic amenities such as water, sanitation, garbage disposal, etc. They generally are not backed by revenue from a specific project.

o Revenue bonds are issued for a specific purpose such as construction of a toll road or a toll bridge.

• Bangalore Municipal Corporation was the first urban local body (ULB) to issue Municipal Bond in India in 1997. **Need for Municipal Bonds**

• Improving urban infrastructure: A High Powered Expert Committee (HPEC) on Urban Infrastructure estimated a requirement of Rs 3.92 million crores to provide urban services conforming to national benchmarks for urban infrastructure over a period 2012-31.

• Alternative source of finance: It may help corporations in raising funds without looking to State grants or agencies such as World Bank. Also, rating agency CARE estimates that large municipalities in India could raise

Rs. 1,000 to Rs. 1,500 crore every year considering municipal bond markets in US and China touch around $3.7 trillion and in China $187 billion.

• Attracting institutional investors: They may ensure participation of large institutional investors such as pension funds and insurance companies by providing less risky avenues of investments to them

Challenges for Municipal Bond Market in India

• Issues with municipal bond: They are relatively less liquid instruments due to absence of secondary market for them, which results in investors having to hold municipal bonds until maturity.

• Credit worthiness: Earlier 94 cities which are part of Smart City Mission and Atal Mission for Rejuvenation and Urban Transformation (AMRUT), were rated by agencies such as CRISIL. Out of 94, 55 cities got investment grade rating (BBB- and above), while other 39 were rated below BBB-. Reasons affecting credit worthiness include:

o Thirteenth finance Commission data reflected that the municipal tax to GDP ratio is a meagre 0.5 per cent as compared to central tax to GDP ratio at 12 per cent.

o Dependence of Municipal bodies for funds and unpredictability of transfers from State governments to ULBs impact the outlook of financial position of ULBs.

• Except in a few big ULBs the budgeting and accounting systems of ULBs still lack transparency which leaves scope for misappropriation of assets and misleading picture of income and expenditure of ULBs.

• There may be increased cases of default when the debts on Municipalities increase too much as is happening in China currently.

• Further there are no insolvency and bankruptcy laws and security enforcement laws applicable against municipalities unlike corporate sector.

Suggestions

• Increasing the marketability of the bonds by bringing them under EEE category (Where the initial investment, the interest earned and the maturity amount are all exempted from taxation) so that retail investors can be brought into the market.

• Need to encourage establishment of bond markets: Creating a secondary market for bond trading to tap long-term savings and allowing households or institutions to sell their long-term bonds before maturity.

• Municipal bonds could be given the status of ‘public securities’ so that they become admissible for statutory liquidity ratio (SLR) investment by commercial banks.

• Further urban infrastructure can be made part of priority sector lending to increase the demand for municipal bonds from institutional investors.

• Introduction of a debt recovery and bankruptcy law applicable to urban entities

• Structural reforms at the governance level must also be undertaken to equip municipalities with the technical and financial expertise to generate adequate credit worthy municipal finance opportunities.

5) OMBUDSMAN SCHEME FOR NON-BANKING FINANCIAL COMPANIES (NBFCS)

The Reserve Bank of India (RBI) has extended the coverage of Ombudsman Scheme for Non-Banking Financial Companies (NBFCs), 2018 to eligible Non Deposit Taking Non Banking Financial Companies (NBFCNDs).

• The coverage will be extended to Non Deposit Taking Non Banking Financial

Companies having asset size of Rs 100 crore or above with customer interface.

• However, Non Banking Financial Company-Infrastructure Finance Company (NBFC-IFC), Core Investment Company (CIC), Infrastructure Debt Fund-Non-banking Financial Company (IDF-NBFC) and NBFCs under liquidation are excluded from the ambit of the Scheme.

Background:

• The Reserve Bank of India (RBI), in February 2018, issued an ombudsman scheme for non-banking finance companies (NBFCs), offering a grievance redressal mechanism for their customers.

Who will be the ombudsman?

• An officer at the RBI not below the rank of general manager will be appointed by the regulator as the ombudsman with territorial jurisdiction being specified by the central bank. The tenure of each ombudsman cannot exceed three years and can be reduced by the regulator if needed.

Who can file the complaint?

• Any customer or person can file a compliant with the ombudsman on various grounds like non-payment or inordinate delay in payment of interest, non-repayment of deposits, lack of transparency in loan agreement, non-compliance with RBI directives on fair practices code for NBFCs, levying of charges without sufficient notice to the customers and failure or delay in returning the securities documents despite repayment of dues among others. Only written complaints or those in electronic format will be accepted.

Appeal:

• If a complaint is not settled by agreement within a specified period as the ombudsman may allow the parties, he may, after affording the parties a "reasonable opportunity to present their case, either in writing or in a meeting, pass an award either allowing or rejecting the complaint".

• The scheme also allows a person to appeal in case of dissatisfaction with any award by the ombudsman.

Compensation:

• The ombudsman may also award compensation not exceeding one hundred thousand rupees to the complainant, taking into account the loss of time, expenses incurred, harassment and mental anguish suffered by the complainant.

Report:

• The ombudsman will be required to send a report to the RBI governor annually on 30 June containing general review of the activities of his office during the preceding financial year and other information required by the central bank.

6) NATIONAL HOUSING BANK

The Reserve Bank of India (RBI) has sold its entire stakes in the National Bank for Agriculture & Rural Development (NABARD) and National Housing Bank. The decision to divest its entire stake was taken based on the recommendations of the second Narasimham Committee.

• The government now holds a 100 per cent stake in both NHB and NABARD.

About NHB:

• NHB is an All India Financial Institution (AIFl), set up in 1988, under the National Housing Bank Act, 1987.

• It is an apex agency established to operate as a principal agency to promote housing finance institutions both at local and regional levels and to provide financial and other support incidental to such institutions and for matters connected therewith.

NABARD:

• It is an apex development and specialized bank established on 12 July 1982 by an act by the parliament of India.
• Its main focus is to uplift rural India by increasing the credit flow for elevation of agriculture & rural non farm sector.
• It was established based on the recommendations of the Committee set up by the Reserve Bank of India (RBI) under the chairmanship of Shri B. Shivaraman.
• It replaced the Agricultural Credit Department (ACD) and Rural Planning and Credit Cell (RPCC) of Reserve Bank of India, and Agricultural Refinance and Development Corporation (ARDC).
• It has been accredited with "matters concerning policy, planning and operations in the field of credit for agriculture and other economic activities in rural areas in India".

7) IMPACT OF CRUDE OIL PRICE RISE ON THE INDIAN RUPEE

Concerns:
• A rise in the price of crude oil hurts the economy because crude accounts for a significant portion of India's overall imports.
• If crude rises further, it will not only impact the stability of the rupee and the rise in stock markets, but may also produce an inflationary effect.

What is leading to the rise in the price of Brent crude?
• The recent spike in prices followed reports that the United States will stop granting sanction waivers to any country importing Iranian crude or condensate beginning May 2, 2019.
• Besides, crude oil prices have been rising steadily since March, 2019 on concerns over supply from OPEC, and the US sanctions on Venezuela.

What is the impact on the rupee? Could it weaken further?
• Inflow of funds from foreign portfolio investors led to a strong recovery in the rupee between January and March 2019. However, the rupee has been rising against the dollar since the reversal in the trend of crude prices.
• If Brent continues to rise, the rupee is likely to face additional pressure. Crude has traditionally been a big determinant of the way the rupee moves.

How it affects economy's?
• A weak rupee hurts the country on account of the higher import bill and current account deficit, and also tends to be inflationary.

Does the US decision on Iran hurt India's imports?
• The US decision to end waivers for countries importing crude from Iran beginning May 2, 2019 may hurt India's interests, as it will have to look for alternative sources of oil.
• It is important to note that the US sanctions on Venezuela are already restrictive for India.
• From April 2018 to January 2019, India imported almost 6.4% of its requirement from Venezuela.
• Also, if the total supplies from these two big oil exporters is kept out of the market, it will lead to a supply crunch, and likely increase in overall crude oil prices.

What are the other sources of crude oil for India?
• While Iraq is the biggest exporter, Saudi Arabia is a close second, and both of them account for 38% of India's total petroleum imports.
• UAE and Nigeria together account for 16.7%.
• However, the biggest change has been the entry of the US as a major player.
• While it did not figure in the list of top 10 petroleum exporters for India in 2017-18, in

the 10 months of FY'19, the US stood at number 9 with an over 3% share of India's petroleum imports.

8) PROFIT ATTRIBUTION TO PERMANENT ESTABLISHMENT (PE) IN INDIA

CBDT invites stakeholder comments on report pertaining to Profit Attribution to Permanent Establishment (PE) in India.

Background:

• Recognizing the significance of issues relating to attribution of profits to a permanent establishment as well as the need to bring greater clarity and predictability in the applicable tax regime, a Committee was formed to examine the existing scheme of profit attribution to PE under Article 7 of DTAAs and recommend changes in Rule 10 of the Income-tax Rules, 1962. The Committee has submitted its report and it has been decided to seek suggestions/comments of the stakeholders and the general public.

Relevance of PEs:

• Usually, foreign companies get tax concession under Double Taxation Avoidance Treaties and they pay taxes in their home countries.

• But if they have PEs in India, they should pay taxes for the income they have created in India. Thus, PE makes a foreign companies' Indian income taxable in India.

What is a Permanent Establishment?

• A Permanent Establishment in India is a fixed place of business, wholly or partly carried out by a foreign enterprise operating in India.

• Such fixed place of business can be a branch office, a place of management, a factory, a warehouse, a workshop etc. However the definition of permanent establishment differs in each tax treaty.

Governing provisions:

• Taxation of non-residents in India is governed by the provisions of the Income-tax Act, 1961 ("the Act") and the provisions of the Double Taxation Avoidance Agreement(s) [DTAA(s)] concluded or adopted by the Central Government under the powers conferred under Section 90 or 90A of the Act, respectively.

• The business income of a non-resident can be taxed in India if it satisfies the requisite thresholds provided under the Act as well as the threshold provided in the applicable tax treaty, by a concept of Permanent Establishment (PE).

9) UNIFIED PAYMENTS INTERFACE (UPI)

An analysis of data from the Reserve Bank of India (RBI), the National Payments Corporation of India (NPCI) and some industry players from April 2018 to March 2019 shows that not only is the UPI platform outperforming e-wallets in terms of the value of transactions done, but it is also eating away at e-wallets' market share in specific areas such as person-to-merchant (P2M) transactions.

• Payments made on the UPI platform saw a remarkable growth of over 400% in the April to March period, from a little more than ₹27,000 crore in April 2018 to ₹35 lakh crore in March 2019.

Why UPI is outperforming e- wallets?

• People are changing the way they transact, choosing bank-tobank methods such as the Unified Payments Interface (UPI) over other instruments such as e-wallets. This is because UPI is completely interoperable and as such, it is unique in the world, where you have an interoperable system on the 'send' and 'receive' side.

• The rapid growth of UPI is accompanied by a reasonably strong growth in the value of transactions done using ewallets, but the latter's growth has not taken off much following the fillip it received in the aftermath of demonetisation in November 2016.

How is it unique?

• Immediate money transfer through mobile device round the clock 24x7 and 365 days.

• Single mobile application for accessing different bank accounts.

• Single Click 2 Factor Authentication – Aligned with the Regulatory guidelines, yet provides for a very strong feature of seamless single click payment.

• Virtual address of the customer for Pull & Push provides for incremental security with the customer not required to enter the details such as Card no, Account number; IFSC etc.

• Bill Sharing with friends.

• Best answer to Cash on Delivery hassle, running to an ATM or rendering exact amount.

• Merchant Payment with Single Application or In-App Payments.

• Utility Bill Payments, Over the Counter Payments, Barcode (Scan and Pay) based payments.

• Donations, Collections, Disbursements Scalable.

• Raising Complaint from Mobile App directly.

What is Unified Payments Interface (UPI)?

• Unified Payments Interface (UPI) is a system that powers multiple bank accounts into a single mobile application (of any participating bank), merging several banking features, seamless fund routing & merchant payments into one hood.

• It also caters to the "Peer to Peer" collect request which can be scheduled and paid as per requirement and convenience.

• It is safe as the customers only share a virtual address and provide no other sensitive information.

Participants in UPI:

• Payer PSP.
• Payee PSP.
• Remitter Bank.
• Beneficiary Bank.
• NPCI
• Bank Account holders.
• Merchants

10) WORLD BANK REPORT ON REMITTANCES

World Bank has released its Migration and Development Brief.

Key findings- India specific:

• India is positioned as the world's top recipient of remittances with its diaspora sending USD 79 billion back home in 2018. The remittances in 2018 grew by over 14 percent in India.

• India managed to retain its top spot in remittances by registering a significant flow of remittances from USD 62.7 billion in 2016 to USD 65.3 billion 2017 and to USD 79 billion in 2018, a significant growth over the last three years. • Natural disasters like Kerala floods likely boosted the financial help that migrants sent to their families.

Global findings:

• The remittances to low-and middle-income countries reached a record high of USD 529 billion in 2018, an increase of 9.6 percent from USD 483 billion in 2017.

• Global remittances, including flows to high-income countries, reached USD 689 billion in 2018, up from USD 633 billion in 2017. The overall increase in remittances regionally was driven by a stronger economy and employment situation in the United States and outward flows from few Gulf Cooperation Council (GCC) countries and the Russian Federation.

11) CURRENCY CHEST

The Reserve Bank of India (RBI) has issued guidelines for banks to set up new currency chests.

The guidelines:

1. Area of the strong room/ vault of at least 1,500 sq ft. For those situated in hilly/ inaccessible places, the strong room/ vault area of at least 600 sq ft.
2. The new chests should have a processing capacity of 6.6 lakh pieces of banknotes per day. Those situated in the hilly/ inaccessible places, a capacity of 2.1 lakh pieces of banknotes per day.
3. The currency chests should have Chest Balance Limit (CBL) of Rs 1,000 crore, subject to ground realities and reasonable restrictions, at the discretion of the Reserve Bank.

What are Currency chests?

• Currency chests are branches of selected banks authorised by the RBI to stock rupee notes and coins.

Who determines the number of notes and coins to be printed?

The responsibility for managing the currency in circulation is vested in the RBI.

• The central bank advises the Centre on the number of notes to be printed, the currency denominations, security features and so on. The number of notes that need to be printed is determined using a statistical model that takes the pace of economic growth, rate of inflation and the replacement rate of soiled notes.

• The Government has, however, reserved the right to determine the amount of coins that have to be minted.

Role of currency chests:

• The RBI offices in various cities receive the notes from note presses and coins from the mints. These are sent to the currency chests and small coin depots from where they are distributed to bank branches.

• The RBI has set up over 4,075 currency chests all over the country. Besides these, there are around 3,746 bank branches that act as small coin depots to stock small coins.

12) CHANGES IN E-WAY BILL SYSTEM

Recently the Finance Ministry has introduced changes in the e-way bill system to crack down on GST evaders.

• With various instances of malpractices in e-way bill generation getting detected, the Government decided to rework the system for generation of e-way bill by transporters and business. During April-December 2018, 3,626 cases of GST evasion involving ₹15,278 crore were detected.

• Important Changes introduced: o Auto-calculation of distance between the source and destination, based on the PIN codes. o Blocking generation of multiple bills based on one invoice. It would permit extension of validity of the e-way bill when the goods are in transit/movement.

About e-way bill

• E-way bill or Electronic-way bill is a document introduced under the GST regime that needs to be generated before transporting or shipping goods worth more than INR 50,000 within state or inter-state.

• It was rolled out on April 1, 2018, for moving goods from one state to another however for intra-state movement of goods it was rolled out in a phased manner.

• The physical copy of e-way bill must be present with the transporter or the person in charge of the conveyance and should include information such as goods, recipient, consignor and transporter.

• Upon generation of the E-Way Bill, on the common portal, a unique E-Way Bill number called 'EBN' is made available to the supplier, the recipient and the transporter.

• The portal has been developed by the National Informatics Centre (NIC).

13) CIRCULAR TRADING

Recently Mumbai High Court granted bail to those arrested for circular trading and evasion of GST.

What is circular trading?

• Circular trading refers to selling and buying of goods via shell corporations to artificially inflate turnover. There is no actual change in ownership or movement of goods.

• For example, a company "A" sold goods to another company "B", which sold the same goods to another company "C". Now, the third company "C" sold the goods to the first company "A". All this while, the goods were kept at a godown of first company.

• Here GST credits were paid on every lap of transaction. The series of sales helped the firms inflate turnover and avail larger valuations and loans. This amounts to tax evasion.

• This is illegal under Prohibition of Fraudulent and Unfair Trade Practices Regulations issued by SEBI. Ketan Parekh stock market scam of 1999 was also related to circular trading.

14) WAYS & MEANS ADVANCES

RBI, in consultation with Government of India, has decided that limits for Ways & Means Advances (WMA) for H1 of FY 2019-20 (April to September 2019) will be Rs 75000 crore. About Ways & Means Advances (WMA)

• The Ways & Means Advances Scheme which commenced in 1997 was designed to meet temporary mismatches in the receipts and payments of the central & state government.

• Under the WMA system, the Reserve Bank extends short-term advances up to the pre-announced half-yearly limits, fully payable within three months.

• Interest rate for WMA is currently charged at the repo rate.

• The limits for WMA are mutually decided by the RBI and the Government of India.

• Overdrafts are allowed at an interest rate 2% above the repo rate, if WMA limits are breached. They cannot be extended beyond 10 consecutive working days.

• When 75% of the limit of WMA is utilised by the government, the RBI may trigger fresh flotation of market loans. • Under the WMA scheme for the State Governments, there are two types of WMA – Special and Normal WMA. o Special WMA is extended against the collateral of the government securities held by the State Government.

o After the exhaustion of the Special WMA limit, State Government is provided a Normal WMA which are unsecured advances at bank rate (Marginal Standing Facility). Normal WMA limits are based on three-year average of actual revenue and capital expenditure of the state.

• Whenever the government resorts to WMA, it effectively also adds to the liquidity in the system.

Government Securities

• A Government Security (G-Sec) is a tradeable instrument issued by the Central Government or the State Governments. It acknowledges the Government's debt obligation.

• Such securities are:

o Short term (usually called treasury bills, with original maturities of less than one year)

o Long term (usually called Government bonds or dated securities with original maturity of one year or more)

• In India, the Central Government issues both, treasury bills and bonds or dated securities while the State Governments issue only bonds or dated securities, which are called the State Development Loans (SDLs).

• G-Secs carry practically no risk of default and, hence, are called risk-free gilt-edged instruments.

15) SMALL FINANCE BANKS

Recently data from the Reserve Bank of India (RBI) show that the small finance bank sector has been seeing remarkable growth in credit disbursement as well as deposits.

About Small Finance Banks (SFBs)

• These are private financial institution for the objective of financial inclusion without any restriction in the area of operations, unlike the Regional Rural Banks or Local Area Banks.

• They can provide basic banking services like accepting deposits and lending to the unbanked sections such as small farmers, micro business enterprises, micro and small industries and unorganised sector entities.

• Some of the operational Small Finance Banks in India are: Ujjivan SFB, Janalakshmi SFB, Equitas SFB, AU SFB, and Capital SFB.

• They were proposed by the Nachiket Mor Committee of RBI, as one of the differentiated banking system for credit outreach and announced in the annual Budget of 2014.

• Currently, SFBs constitutes 0.2% of the total deposits of all scheduled commercial banks and makes up 0.6% of the total lending undertaken by the scheduled commercial banks in India.

Need for Small Finance Banks

• Differentiated banking to cater large population: India has second-largest unbanked population in the world where more than 200 million people do not have a bank account and many rely on cash or informal financing. Therefore, SFBs provide access to finance to a large unbanked population. • Priority sector lending: SFBs play a key role in the priority sector lending space as their main focus is the unserved and underserved segment.

• Financial inclusion of women: Most of the Small Finance Banks were earlier microfinance companies - to provide loans to women. Now that these have become a bank, female customers can avail full banking solutions. Also, through different CSR initiatives, Small Finance Banks reach out to women customers and make them understand the need of financial planning and banking services.

• Social Impact: The SFBs are now looking beyond the simple metric of "income improvement" to other indicators of positive social impact, like customer employment characteristics, customer distribution between urban and rural markets and women's engagement. SFBs not only serve to provide banking solutions but empower the socio-economic progress of its consumers. RBI states that small banks will act as a savings vehicle to these segments of the population.

Regulations for SFBs

• They cannot set up subsidiaries to undertake non-banking financial service activities.

• They have Minimum paid-up equity capital requirement of Rs 100 crore.

• The promoter's minimum initial contribution to the paid-up equity capital of such bank shall at least be 40% which can be gradually brought down to 26% within 12 years from the date of commencement of operations

• 75% of its Adjusted Net Bank Credit (ANBC) should be advanced to the priority sector as categorized by RBI.

• It must have 25% of its branches set up in unbanked areas.

• Maximum loan size to a single person cannot exceed 10% of total capital funds; cannot exceed 15% in the case of a group.

• They can undertake financial services like distribution of mutual fund units, insurance products, pension products, and so on, but not without prior approval from the RBI.

• They will be subject to all prudential norms and regulations of the RBI as applicable to existing commercial banks. For ex: maintaining cash reserve ratio (CRR) and statutory liquid ratio (SLR).

• It can transform into a full-fledged bank, but only after RBI's approval.

Differentiated Banks

• They are banking institutions licensed by the RBI to provide specific banking services and products.

• Main aim for giving license to these banks is to promote financial inclusion and payments.

• Differentiated banks licensing was launched in 2015.

• They are of two types-Payment banks and Small finance banks.

16) CAPITAL ACCOUNT LIBERALISATION

Recently, RBI's Deputy Governor has argued in favour of revisiting India's policies with respect to Capital Account Liberalisation.

About Capital Account Liberalisation

• Foreign exchange transactions are broadly classified into two types: Current account transactions and Capital account transactions.

o The Current Account represents a country's current transactions including exports, imports, interest payments, private remittances and transfers.

o The Capital Account records the net change of assets and liabilities which include external lending and borrowing, foreign currency deposits of banks, external bonds issued by the Government of India, Foreign Direct Investment (FDI), Foreign Portfolio Investments in India (FPI) etc.

• In the early nineties, India's foreign exchange reserves were so low that these were not enough to pay for a few weeks of imports. Hence, India initiated reforms in Foreign transactions and in 1994, India allowed full current account convertibility in 1994. However, capital account transactions were not made fully convertible.

• Currency convertibility refers the ease with which a country's currency can be converted into gold or another currency in global exchanges. It indicates the extent to which the regulations allow inflow and outflow of capital to and from the country. Thus, for-

o Current Account- Indian rupee can be converted to any foreign currency at existing market rates for trade purposes for any amount.

o Capital Account- It means that ease with which, the foreign investors will be able to buy Indian assets such as bonds, equity and

Indian citizens will be able to buy foreign financial assets.

• Since, the last decade, the government and the central bank have been exploring ways and trajectory in which fuller capital account convertibility could be achieved.

Arguments in favour of Capital Account Liberalisation

• Bring in financial efficiency- An open capital account could bring with it greater specialisation and innovation by exposing the financial sector to global competition.

• Can attract larger foreign capital- where external capital can supplement the domestic saving in the effort to mobilize resources for welfare and infrastructure.

• Increase the choices for investments- Residents get the opportunity to base their investment and consumption decisions on world interest rates and world prices for tradeables, which could enhance their interests and welfare. • Improves competitive discipline- By offering the opportunity of using the world market to diversify portfolios, an open capital account permits both savers and investors to protect the real value of their assets through risk reduction.

• Helps complement current account- Capital controls are not very effective, particularly when current account is convertible, as current account transactions create channels for disguised capital flows.

• Changed global scenario- Capital controls are there to insulate domestic financial conditions from external financial developments. The influence of external financial conditions, however, has been increasing over the years even in countries with extensive capital controls and because the costs of evading the controls have declined and the attractiveness of holding assets in offshore markets have increased, capital controls are increasingly becoming ineffective.

Arguments against Capital Account Liberalisation

• Could lead to the export of domestic savings- which can further erode the capacity of state to finance the national imperatives.

• Could lead to greater tax avoidance- It would weaken the ability of the authorities to tax domestic financial activities, income and wealth.

• Could expose the economy to greater macroeconomic instability- arising from the volatility of short-term capital movements, the risk of large capital outflows and associated negative externalities.

• Premature liberalisation- could initially stimulate capital inflows that would cause real exchange rate to appreciate and thereby destabilise an economy undergoing the fragile process of transition and structural reform. Once stabilisation programme lacks credibility, currency substitution and capital flight could trigger a Balance of Payment crisis, depreciation and spiraling inflation.

• May lead to ineffective monetary policy- due to speculative short-term movements in the interest rates, leading to other spiraling effects.

• Due to higher capital inflows following capital convertibility, the appreciating real exchange rate would divert resources from tradable to non-tradable sectors (like construction, housing, hotels and tourism etc.) and this would happen in the face of rising external liabilities ("Dutch disease effect").

• Could lead to financial bubbles- especially through irrational exuberance of investment in real estate and equity market financed by unbridled foreign borrowing.

Benefits of Capital Account Convertibility

• Creating overseas assets- currently is seen as a measure of dividend earning, rather it could be looked as value enhancement.

• Acquisition of assets- which are of strategic and economic importance, such as coalfields, oilfields etc. can bring long term dividends.

• Relocation of Start-ups- are using the holding company structure to invest in India because of the ease of raising capital in a foreign jurisdiction. This can be corrected and Start-ups can relocate in India.

• Greater technological and strategic investments in India- such as by defence companies, research companies etc.

Way Forward

• Given the trade-off between growth/efficiency and stability associated with capital flows, India's preference has strongly been in favour of avoidance of instability. Such an approach has imparted stability not only to the financial system but also to the overall growth process.

• The relative weights to efficiency and stability need to be constantly reviewed in the view of contemporary developments.

• While realizing that the impulses of growth could be supplemented with foreign capital, it is imperative to ensure that liberalisation of the capital account responds to the requirement of the economy in an appropriate, gradual and cautious manner.

Committees on Capital Account Convertibility (1997, 2006)

• The Reserve Bank of India setup committees on capital account convertibility under the chairmanship of S.S. Tarapore in 1997 and 2006 respectively.

• The committee had supported the idea of full convertibility in the capital account. It recommended this to be done in a phased manner and subject to certain preconditions.

• Some pre-conditions are-

o Fiscal Stability- low fiscal deficit

o Price Stability- low inflation

o Stability of financial institutions and markets

o Low Non-Performing Assets

Present Capital Controls in Indian Economy

• Capital control represents any measure taken by a government, central bank or other regulatory bodies to limit the flow of foreign capital in and out of the domestic economy.

• Some of the controls used presently are-

o Cap on total FPIs in domestic securities with separate limits on different kinds of them.

o Cap on External Commercial Borrowings (ECBs) and Masala Bonds together.

o Restrictions on investors by their horizon of investment, such as, Insurance firms, Endowments and Pension Funds etc.

o Restrictions on maturity of the underlying investment.

o Restrictions to ensure that only relatively high credit quality borrowers tap into ECBs.

17) ASIAN DEVELOPMENT OUTLOOK 2019

ADB publishes Asian Development Outlook 2019.

Key findings:

• Growth in developing Asia is projected to soften to 5.7% in 2019 and 5.6% in 2020. Excluding Asia's highincome newly industrialized economies, growth is expected to slip from 6.4% in 2018 to 6.2% in 2019 and 6.1% in 2020.

• Since oil prices rose and Asian currencies depreciated, inflation edged up last year but remained low by historical standards. In light of stable commodity prices, inflation is anticipated to remain subdued at 2.5% in both 2019 and 2020.
• Only 20 of 45 individual economies are projected to see growth accelerate in 2019.
• By sub-region, aggregate growth rates in Central Asia, East Asia, and Southeast Asia are expected to decelerate, while South Asia and the Pacific will bounce back from slowdown in 2018.
• In East Asian economy growth in East Asia decelerated by 0.2% to 6.0% in 2018, weighed down by weakening external trade and moderating investment in the People's Republic of China (PRC) but sustained by resilient domestic consumption.

India's position:

• Growth rate: India's growth forecast is cut to 7.2% for 2019-20 because of a slower-than-expected pickup in investment demand. The growth rate in Financial Year 2020-21 is likely to be 7.3%.
• Recovery may be due to– agriculture and stronger domestic demand, improved health of banks and corporations and implementation of a value-added tax.
• The inflation is expected to average around 4% in the first half of FY2019, and therefore the Reserve Bank would have some room for lowering policy rates further increasing credit.

About ADB:

• The Asian Development Bank was conceived in the early 1960s as a financial institution that would be Asian in character and foster economic growth and cooperation in one of the poorest regions in the world.
• It assists its members, and partners, by providing loans, technical assistance, grants, and equity investments to promote social and economic development.
• Established on 19 December 1966.
• Headquartered — Manila, Philippines.
• Official United Nations Observer.

Voting rights:

• It is modelled closely on the World Bank, and has a similar weighted voting system where votes are distributed in proportion with members' capital subscriptions.
• Japan > United States > China > India > Australia

18) SUPREME COURT STRIKES DOWN RBI CIRCULAR ON DEBT RESOLUTION

The Supreme Court of India on April 2, 2019 struck down the Reserve Bank of India's February 2018 order on non-performing assets, as a result of which all cases referred to or admitted under the Insolvency and Bankruptcy Code (IBC) due to the RBI order would now be cancelled.

Background:

• The apex court struck down the controversial RBI circular mandating resolution of loans of Rs 2,000 crore and above even for a single day as ultra vires.
• The judgement was pronounced on a batch of petitions filed by various industries including power, fertiliser and sugar, challenging the February order.

What did the court rule?

• The Supreme Court held the February 12 circular "ultra vires as a whole" — essentially meaning the RBI had gone beyond its powers — and thus "of no effect in law".

Impacts of the order:

• Following the Supreme Court order, all the companies either referred or admitted for the resolution process, whichever stage of the proceedings they are, would be treated as they were never referred for insolvency.

• The decision would benefit various sectors that are facing stress including power, sugar and shipping and those companies, which were facing difficulties in honouring their loan commitments.

• However, power companies, including 34 stressed projects with a capacity of about 40,000 MW would be the biggest beneficiaries as it now provides both banks and power generators with more time to resolve their debt.

What necessitated this?

• The decision comes after several power companies had moved the top court in August, challenging the constitutional validity of the February 12 RBI circular.

• The power sector had contended that they were not willful defaulters and were facing sectoral and market issues, including non-availability of fuel and power purchase agreement (PPAs) and non-payment by state utilities issues.

• They had stated that this hampered their ability to generate revenue and maintain their loan repayment schedule with banks.

What was the circular all about?

1. The February 12, 2018 RBI circular had asked banks and other lenders to either execute a resolution plan for big stressed accounts or file insolvency petitions against them in the National Company Law Tribunal (NCLT).
2. As per the circular, 34 power companies were declared stressed by the standing committee on energy and some of them were referred for insolvency under the new bankruptcy code.
3. The RBI had allowed 180 days for debt resolution, failing which the asset would have to be taken to NCLT for initiation of insolvency against them. The deadline for the same had been fixed for August 31, 2018.

Need for the circular:

• Recognising defaults by Banks: The circular had forced banks to recognise defaults by large borrowers with dues of over ₹2,000 crore within a day after an instalment fell due. And if not resolved within six months after that, they had no choice but to refer these accounts for resolution under the Insolvency and Bankruptcy Code.

• Increasing share of Bad loans: Mounting bad loans, which crossed 10% of all advances at that point. The failure of existing schemes such as corporate debt restructuring, stressed asset resolution and the Scheme for Sustainable Structuring of Stressed Assets (S4A) to make a dent in resolving them formed the backdrop to this directive.

• Breaking nexus: The circular was aimed at breaking the nexus between banks and defaulters, both of whom were content to evergreen loans under available schemes.

• Introducing Credit Discipline: It introduced a certain credit discipline — banks had to recognise defaults immediately and attempt resolution within a six-month timeframe, while borrowers risked being dragged into the insolvency process and losing control of their enterprises if they did not regularise their accounts.

Way forward:

• It is now important for the central bank to ensure that the discipline in the system does not slacken.

• The bond market does not allow any leeway to borrowers in repayment, and there is no reason why bank loans should be any different.

• The RBI should study the judgment closely, and quickly reframe its guidelines so that they are within the framework of the powers available to it under the law.

• Else, the good work done in debt resolution in the last one year will be undone.

19) ADVANCE PRICING AGREEMENTS (APAS)

The Central Board of Direct Taxes (CBDT) has entered into 18 Advance Pricing Agreements (APAs) in March this year, including three bilateral APAs.

• With the signing of these APAs, the total number of APAs entered into by the CBDT in the year 2018-19 stands at 52, which includes 11 bilateral APAs. The total number of APAs entered into by the CBDT as of now stands at 271, which inter alia includes 31 bilateral APAs.

What are APAs?

• An APA is an agreement between a taxpayer and the tax authority determining the Transfer Pricing methodology for pricing the tax payer's international transactions for future years. An APA provides certainty with respect to the tax outcome of the tax payer's international transactions. An APA can be one of the three types – unilateral, bilateral and multilateral.

1. A Unilateral APA is an APA that involves only the taxpayer and the tax authority of the country where the taxpayer is located.
2. Bilateral APA (BAPA) is an APA that involves the tax payer, associated enterprise (AE) of the taxpayer in the foreign country, tax authority of the country where the taxpayer is located and the foreign tax authority.
3. Multilateral APA (MAPA) is an APA that involves the taxpayer, two or more AEs of the tax payer in different foreign countries, tax authority of the country where the taxpayer is located and the tax authorities of AEs.

Significance:

• The progress of the APA scheme strengthens the government's resolve of fostering a non-adversarial tax regime. The Indian APA programme has been appreciated nationally and internationally for being able to address complex transfer pricing issues in a fair and transparent manner.

20) PURCHASING MANAGERS INDEX (PMI)

What is a PMI?

• PMI or a Purchasing Managers' Index (PMI) is an indicator of business activity — both in the manufacturing and services sectors.

• It is a survey-based measures that asks the respondents about changes in their perception of some key business variables from the month before.

• It is calculated separately for the manufacturing and services sectors and then a composite index is constructed.

How is the PMI derived?

• The PMI is derived from a series of qualitative questions. Executives from a reasonably big sample, running into hundreds of firms, are asked whether key indicators such as output, new orders, business expectations and employment were stronger than the month before and are asked to rate them.

How does one read the PMI?

• A figure above 50 denotes expansion in business activity. Anything below 50 denotes contraction. Higher the difference from this mid-point greater the expansion or contraction. The rate of expansion can also be judged by comparing the PMI with that of the previous month data.

• If the figure is higher than the previous month's then the economy is expanding at a faster rate. If it is lower than the previous month then it is growing at a lower rate.

What are its implications for the economy?

• The PMI is usually released at the start of the month, much before most of the official data on industrial output, manufacturing and GDP growth becomes available.

• It is, therefore, considered a good leading indicator of economic activity. Economists consider the manufacturing growth measured by the PMI as a good indicator of industrial output, for which official statistics are released later. • Central banks of many countries also use the index to help make decisions on interest rates.

What does it mean for financial markets?

• The PMI also gives an indication of corporate earnings and is closely watched by investors as well as the bond markets. A good reading enhances the attractiveness of an economy vis-a- vis another competing economy.

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