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CHAPTER-2

HISTORICAL BACKGROUND

2.1 Historical perspective

In 1948, immediately after Independence, Government introduced the Industrial Policy Resolution. This outlined the approach to industrial growth and development. It emphasized the importance to the economy of securing a continuous increase in production and ensuring its equitable distribution. After the adoption of the Constitution and the socio-economic goals, the Industrial Policy was comprehensively revised and adopted in 1956. To meet new challenges from time to time, it was modified through statements in 1973, 1977 and 1980. [6]

The Industrial Policy Resolution of 1948 was followed by the Industrial Policy Resolution of 1956, which had as its objective the acceleration of the rate of economic growth and the speeding up of industrialization as a means of achieving a socialist pattern of society. In 1956, capital was scarce and the base of entrepreneurship not strong enough. Hence the 1956 Industrial Policy Resolution gave primacy to

[6] *Government of India, available at www. siadipp.nic.in/publicat/nip0791.htm, last visited on 12/10/2009*

the role of the State to assume a predominant and direct responsibility for industrial development. [7]

The Industrial Policy Statement of 1973, inter alias, identified high priority industries where investment from large industrial houses and foreign companies would be permitted. The Industrial Policy Statement of 1977 laid emphasis on decentralization and on the role of small-scale, tiny and cottage industries.

The Industrial Policy Statement of 1980 focused attention on the need for promoting competition in the domestic market, technological up gradation and modernization. The policy laid the foundation for an increasingly competitive export base and for encouraging foreign investment in high-technology areas. This found expression in the Sixth Five-Year Plan, which bore the distinct stamp of Mrs. Indira Gandhi. It was Mrs. Gandhi who emphasized the need for productivity to be the central concern in all economic and production activities. [8]

These policies created a climate for rapid industrial growth in the country. Thus, on the eve of the Seventh Five-Year Plan a broad-based infrastructure had been built up. Basic industries had been established. A high degree of self-reliance in a large number of items--raw materials,

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[7] *Ibid 6*

[8] *Timeline history for Industrial Policy Resolution, available at www.google.b..ks.com , last visited on 4/10/09*

intermediates, and finished goods had been achieved. New growth centre of industrial activity had emerged, as had a new generation of entrepreneurs. A large number of engineers, technicians and skilled workers had also been trained. [9]

The Seventh Plan recognized the need to consolidate on these strengths and to take initiatives to prepare Indian industry to respond effectively to the emerging challenges. A number of policy and procedural changes were introduced in 1985 and 1986 under the leadership of Mr. Rajiv Gandhi aimed at increasing productivity, reducing costs and improving quality. The accent was on opening the domestic market to increased competition and readying our industry to stand on its own in the face of international competition.

The public sector was freed from a number of constraints and given a larger measure of autonomy. The technological and managerial modernization of industry was pursued as the key instrument for increasing productivity and improving our competitiveness in the world. The net result of all these changes was that Indian industry grew by an impressive average annual growth rate of 8.5 per cent in

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[9] *Industrial policy in India, issues, Policy and objectives, available at www.uneca.org/aida/documents/Industrial%20Policies_India.ppt, last visited on 5/10/09*

the Seventh Plan period and it enjoyed the same success on Germany and Japan. [10]

Government is pledged to launching reinvigorated struggle for social and economic justice, to end poverty and unemployment and to build a modem, democratic, socialist, prosperous and forward-looking India. Such a society can be built if India grows as part of the world economy and not in isolation.

While Government will continue to follow the policy of self-reliance, there would be greater emphasis placed on building up our ability to pay for imports through our own foreign exchange earnings. Thus the overall purpose is to coordinate the efforts of private sector and public sector and to develop their new technologies. [11]

Government will continue to pursue a sound policy framework encompassing encouragement of entrepreneurship, development of indigenous technology through investment in research and development, bringing in new technology, dismantling of the regulatory system, development of the capital markets and increasing competitiveness for the benefit of the common man. The spread of industrialization to backward areas of the country

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[10] *See, Industrial Policy at www. answeres.com/topic/industrial policy, last visited on 2/9/09*

[11] *Ibid 10*

will be actively promoted through appropriate incentives, institutions and infrastructure investments. [12]

Government will provide enhanced support to the small-scale sector so that it flourishes in an environment of economic efficiency and continuous technological up gradation. Foreign investment and technology collaboration will be welcome to obtain higher technology, to increase exports and to expand the production base. [13]

Government will endeavor to abolish the monopoly of any sector or any individual enterprise in any field of manufacture, except on strategic or military considerations and open all manufacturing activity to competition.

Government will ensure that the public sector plays its rightful role in the evolving socio-economic scenario of the country. Government will ensure that the public sector is run on business lines as envisaged in the Industrial Policy Resolution of 1956 and would continue to innovate and lead in strategic areas of national importance. In the 1950s and 1960s, the principal instrument for controlling the commanding heights of the economy was investment in the capital of key industries. Today, the State has other instruments of intervention, particularly fiscal and monetary instruments. The State also commands the bulk of the

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[12] *Ref. Material of IGNOU, Unit 17, India's External Debt*
[13] *Ibid 12*

nation's savings. Banks and financial institutions are under State control. Where State intervention is necessary; these instruments will prove more effective and decisive. [14]

Government will fully protect the interests of labour, enhance their welfare and equip them in all respects to deal with the inevitability of technological change. Government believes that no small section of society can corner the gains of growth, leaving workers to bear its pains. Labour will be made an equal partner in progress and prosperity. Workers' participation in management will be promoted. Workers co-operatives will be encouraged to participate in packages designed to one word turn around sick companies. Intensive training, skill development and up gradation programmers will be launched.

Government will continue to visualize new horizons. The Major objectives of the new industrial policy package will be to build on the gains already made, correct the distortions or weaknesses that may have crept in, maintain a sustained growth in productivity and gainful employment and attain international competitiveness. The pursuit of these objectives will be tempered by the need to preserve the environment and ensure the efficient use of available resources. All sectors of industry whether small, medium or large, belonging to the public, private or cooperative sector

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[14] *Ibid 12*

will be encouraged to grow and improve on their past performance.[15]

Government's policy will be continuity with change.
In pursuit of the above objectives, the Government has decided to take a series of initiatives in respect of the policies relating to the following areas.

- Industrial Licensing
- Foreign Investment
- Foreign Technology Agreements
- Public Sector Policy
- MRTP Act.

A package for the small and tiny sectors of Industry is being announced separately

2.2 Historical Backgrounds: Indian, Ancient, Medieval, Modern

The British rulers used centralization to secure a hold on the rulers of India and to fulfill their commercial interest. This framework remained in place even after Independence, the consequence of which has been vividly described. The noteworthy aspect of this treatise is the lucid description of the entrepreneurship and commercial adventure under the colonial rule, the effect of industrial revolution and later on globalization which provided the backdrop to development in India since it achieved Independence. Thus Industrial

[15] *Ibid 12*

Revolution changed the world in a manner that very few other developments in the world have. [16]

The various topics under the 'Current Trends' forcibly brings out the challenges that will arise in the new millennium in the development of Industries and the methods to overcome those obstacles. The detailed analysis of the set up and management functioning of private entrepreneurship companies reveals their strength and weaknesses. How the public sector units played an important role after the dawn of Independence, their present performances and the ways and means to improve their functioning will act as a good guide to the mangers of PSUs.

Though has suggested disinvestment and privatization of PSUs to meet challenges of globalization and the guidelines of the WTO regime, he is fully aware that such a step may not be essential for profit-making PSUs. [17]

Having commented on current trends in trade industries let us revert back to the Indus Valley civilization of 3000 BC and the trade links developed during that period extending up to early Christian era. He dwells on various challenges in cultural ties starting from the days of Harappan culture and the resultant trade link India developed with Europe,

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[16] *See Effects if Industrial Revolution, available at http://www.buzzle.com/articles/effects-of-industrial-revolution.html, last visited on 4/11/09*
[17] *Ibid16*

Arabia, the Middle East and the Far East. At the start of Christian era there was good trade growth with Rome. Vast potentials were developed for trading through sea and land routes. Principal commodities that were traded during that period were identified as spices, silk, precious stones, areca nut, sandal-wood, gold, silver, pearls, corals etc.

Indian trade with other countries flourished during the Mauryan and the Gupta periods. As India lies along the route between the West and the Far East, several Indian cities had developed well-established trade links with the West and the East. Pataliputra, Kaveipatta, Taxila, Saketa, Mithila, Ujaain, Kanchi, Madura, Broach, Mathura, and Tamraplipta were some of the leading commercial centers in ancient India. [18]

The true aspect of Chanakya

The momentous life of Chanakya reminds us of a revengeful saga where the individual is obsessed by the idea of taking revenge. But personal revenge was not the aim of Chanakya. He wanted that the kingdom should be secure and that the administration should go on smoothly, bringing happiness to the people. He thought that there were two ways of ensuring the happiness of the people. Firstly, Amatya Rakshasa had to be made Chandragupta's minister, Secondly, a book must be written, laying down

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[18] *Ibid 16*

how a king should conduct himself, how he should protect himself and the kingdom from the enemies, how to ensure law and order, and so on.

By writing "Arthashastra" and "Nitishastra", Chanakya has become a never ending phenomenon. He has truly guided the generations with his wisdom. It would ideally suit the closing of the life of Chanakya with a couple of quotations by Chanakya "The secret task of a king is to strive for the welfare of his people incessantly. The administration for the kingdom is his religious duty. His greatest gift would be to treat all as equals." His works were lost near the end of the Gupta dynasty and not rediscovered until 1915 [19]

"The happiness of the commoners is the happiness of the king. Their welfare is his welfare. A king should never think of his personal interest or welfare, but should try to find his joy in the joy of his subjects."

These words were written 2300 years ago by Chanakya, the expert statesman and wise sage. And Chanakya is also another name for courage and perseverance. [20]

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[19] *See, Chanakya, available at http://en.wikipedia.org/wiki/Chanaky, last visited on 10/12/09*
[20] *Ibid 19*

His dreams

Chanakya envisioned India as a nation which would place itself as the forerunner - politically, economically and socially. His magnum opus, **"Arthashatra", depicts in many ways the India of His dreams.** When he wrote this volume of epic proportion, the country was ridden in production, was in a transitional phase, moving towards the advanced aspects of distribution and production. Culture and regional politics directed the way in which trade was done.

The main activities of the economy were agriculture, cattle rearing and commerce. Among the three, Chanakya considered agriculture to be the most important constituent of the economy. It's a fact today that the Indian economy of today is an agro based one. Covering various topics on administration, politics and economy, it is as book of law and a treatise on running a country which is relevant even today. [21]

People who thing that the society in which we live will remain the same, are dissuading themselves of the truth. Society is a complex and dynamic system changing constantly leaving those people behind who say not to change. Broadly speaking, Chanakya dreamt of a country

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[21] *Ibid 19*

reaching the following levels of development in terms of ideologies and social economic development: [22]

- A self sufficient economy which is not dependent on foreign trade.
- An egalitarian society where there are equal opportunities for all.
- Establishment of new colonies for the augmentation of resources. He also advocated the development of the already annexed colonies. His imperialistic views can be interpreted as the development of natural and man made resources.
- According to Chanakya, the efficient management of land is essential for the development of resources. It is essential that the state keeps and eye on the occupation of excess land by the landlords and unauthorized use of land. Ideally the state should monitor the most important and vital resource – Land.
- The state should take care of agriculture at all times. Government machinery should be directed towards the implementation of projects aimed at supporting and nurturing the various processes, beginning from sowing of seeds to harvest.
- The nation should envisage to construct forts and cities. These complexes would protect country from invasions and provide internal security. The cities

[22] *Ibid 19*

would act as giant markets increasing the revenue of the state.

- Internal trade was more important to Chanakya than external trade. At each point of the entry o goods, a minimal amount of tax should be collected. The state should collect taxes at a bare minimum level, so that there is no chance of tax evasion.
- Laws of the state should be the same for all, irrespective of the person who is involved in the case. Destitute of women should be protected by the society because they are the result of social exploitation and the uncouth behavior of men.
- Security of the citizens at peace time is very important because state is the only savior of the men and women who get affected only because of the negligence of the state. Antisocial elements should be kept under check along with the spies who may enter the country at any time.
- Chanakya envisioned a society where the people are not running behind material pleasures. Control over the sense organs is essential for success in any endeavor. Spiritual development is essential for the internal strength and character for success in any endeavor. Spiritual development is essential for the internal strength and character of the individual. Material pleasures and achievements are always

secondary to the spiritual development of the society and country at large. [23]

During the Mughal period, though Indian trade was flourishing it was captured slowly by the Portuguese, Dutch, and the English. Goa and Calicut respectively were the main trade centers of Portuguese and Dutch. The East India Company started its trade link from Bengal, Masulipatnam in Andhra and Madras in South. The East India Company during the 17th and 18th centuries extended it's sphere of activities to other parts of the county.

A gradual transformation from trading to factory to port and port to political control was the result of the political conditions that were then obtaining in India especially in Eastern markets. In 1757 the English became the real masters of Bengal. Clive started the foundation for English regime. Disunity and quarrels during the late Mughal period and the start of disintegration of small states due to surrender or acceptance to mighty British force led to the establishment of colonial British regime. The emergence of that regime effectively stamped out many of the natural industries of India for the befit of English manufacturers. [24]

In the advent of increasing numbers of Industries, necessity was felt for co-ordination amongst them and also to get

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[23] *Ibid 19*

[24] *S.C. Srivastva, Industrial Relation & Labour laws, Published by Vikas Publications, ed 2005*

concessions from the government. That necessity gave birth to the first chamber of commerce named "The Calcutta Chamber of Commerce" followed by such organization in other metropolitan cities. An apex organization called 'Federation of Indian Chamber of Commerce and Industry'. FICCI was set up in 1927 with Purushottam Das Thakurdas as President and G.D. Birla as its Vice-President. [25]

Growth of public and private sector units, their achievements in improving the economic condition of India, management style etc are discussed in detail and this will be of great interest to all especially the practicing managers of industries. The analysis of industrial group, growth of joint sector companies, details of corporate management and Managing Agency System will give very useful information for improving the present day industrial set up.

Very comprehensively the saga of an important industries such as textile, jute, and the infrastructure industries such as power, road, transport and shipping in regard to their growth, short comings and other related matters. Those details, if fully understood and the suggested recommendations implemented could accelerate their growth. [26]

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[25] *Ibid 24*
[26] *Ibid 24*

Industrial houses in various parts of the country especially the Tatas, Birlas, Mafatlal, Godrej to name a few will be of interest to readers. Financial institutions are the back bone for industrial development. They play a vital role in the economic life of a country. The nationalized and private banks, LIC, UTI and stock exchanges aid the growth of industries. The chapter analyzing the above mentioned financial institutions with detailed statistical figures enables the reader to understand the various economic parameters and gives an idea as to how the country is placed on the economic front.

The outlook of the industrial sector has undergone a qualitative change. India's exports amounted to $18 billion in 1991-92 and in 1999-2000 the merchandise exports amounted to $36.5 billion. To further enhance exports, globalization is inescapable. We can achieve results only if the infrastructure is improved considerably and industrial constraints are regulated.

Commitments in infrastructure such as power, communication, transport, etc can be met with only by increased inflow of funds by assistance of FDI and internal agencies. The joining of the WTO and opening the doors to globalization, though criticized, are necessities for industrial growth and economic development. [27]

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[27] *Ibid 24*

Amartya Sen. has spoken strongly in favor of globalization with a human face; the alternative described by him was to become kupamandu --- a frog in the well. Dr. Agrawala's narrative supports and endorses Prof. Sen.'s view and reinforces the need and necessity for globalization.

2.3 Industrial Licensing Policy

Industrial Licensing is governed by the Industries development & Regulation Act, 1951.

The Industrial Policy Resolution of 1956 identified the following three categories of industries:

- Those that would be reserved for development in the public sector;
- Those that would be permitted for development through private enterprise with or without State participation; and
- Those in which investment initiatives would ordinarily emanate from private entrepreneurs.

Over the years, keeping in view the changing industrial scene in the country, the policy has undergone modifications. Industrial Licensing policy and procedures have also been liberalized from time to time. A full realization of the industrial potential of the country calls for a continuation of this process of change.

In order to achieve the objectives of the strategy for the industrial sector for the 1990s and beyond, it is necessary to make a number of changes in the system of industrial approvals. Major policy initiatives and procedural reforms are called for in order to actively encourage and assist Indian entrepreneurs to exploit and meet the emerging domestic and global opportunities and challenges. The bedrock of any such package of measures must be to let the entrepreneurs make investment decisions on the basis of their own commercial judgment.

The attainment of technological dynamism and international competitiveness requires that enterprises must be enabled to swiftly respond to fast changing external conditions that have become characteristic of today's industrial world.

Government policy and procedures must be geared to assisting entrepreneurs in their efforts. This can be done only if the role played by the Government were to be changed from that of only exercising control to one of providing help and guidance by making essential procedures fully transparent and by eliminating delays. [28]

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[28] *See, Government of India, available at siadipp.nic.in/publicat/nip0791.htm, last visited on 23/12/09*

The winds of change have been with us for some time. The industrial licensing system has been gradually moving away from the concept of capacity licensing. The system of reservations for public sector undertakings has been evolving towards an ethos of greater flexibility and private sector enterprise has been gradually allowed to enter into many of these areas on a case by case basis. Further inputs must be provided to these changes which alone can push this country towards the attainment of its entrepreneurial and industrial potential. This calls for bold and imaginative decisions designed to remove restraints on capacity creation, while, at the same time ensuring that overriding national interests are not jeopardized. [29]

In the above context, industrial licensing will henceforth be abolished for all industries, except those specified, irrespective of levels of investment. These specified industries will continue to be subject to compulsory licensing for reasons related to security and strategic concerning social reasons, problems related to safety and overriding environmental issues, manufacture of products of hazardous nature and articles of elitist consumption.

The exemption from licensing will be particularly helpful to the many dynamic small and medium entrepreneurs who have been unnecessarily hampered by the licensing system. As a whole the Indian economy will benefit by becoming

[29] *Ibid 28*

more competitive, more efficient and modem and will take its rightful place in the world of industrial progress. [30]

2.4 Foreign Investment

While freeing Indian industry from official controls, opportunities for promoting foreign investments in India should also be fully exploited. In view of the significant development of India's industrial economy in the last 40 years, the general resilience, size and level of sophistication achieved, and the significant changes that have also taken place in the world industrial economy, the relationship between domestic and foreign industry needs to be much more dynamic than it has been in the past in terms of both technology and investment.

Foreign investment would bring attendant advantages of technology transfer, marketing expertise, introduction of modern managerial techniques and new possibilities for promotion of exports. This is particularly necessary in the changing global scenario of industrial and economic cooperation marked by mobility of capital. The Government will therefore, welcome foreign investment, which is in the interest of the country's industrial development. [31]

In order to invite foreign investment in high priority industries, requiring large investments and advanced

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[30] *Ibid 28*
[31] *Ibid 12*

technology, it has been decided to provide approval for direct foreign investment up to 51 per cent foreign equity in such industries. There shall be no bottlenecks of any kind in this process. This group of industries has generally been known as the "Appendix I industries" and are areas in which FERA companies have already been allowed to invest on a discretionary basis. This change will go a long way in making Indian policy on foreign investment transparent. Such a framework will make it attractive for companies abroad to invest in India. [32]

Promotion of exports of Indian products calls for a systematic exploration of world markets possible only through intensive and highly professional marketing activities. To the extent that expertise of this nature is not well developed in India, Government will encourage foreign trading companies to assist us in our export activities. Attraction of substantial investment and access to high technology, often closely held, and to world markets, involves interaction with some of the world's largest international manufacturing and marketing firms. The Government will appoint a special board to negotiate with such a firm so that we can engage in purposive negotiation with such large firms, and provide the avenues for large investments in the development of industries and technology in the national interest. [33]

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[32] *Ibid 12*
[33] *Ibid 12*

An industrializing economy like India can greatly benefit in different ways by welcoming foreign capital into the country:

1. India can have better technology to exploit the unutilized and under utilized national resources
2. Foreign investment and technology will enable technology, upgradation and modernization of industry to improve quality and productivity
3. Foreign investment will supplement domestic savings and capital formation towards accelerating the rate of investment for economic development
4. Foreign investment and technology will help to build up the much needed infrastructure for the development of agriculture and industry
5. Foreign investment will bring marketing expertise which would enable Indian goods to penetrate the international market on a larger scale
6. Foreign investment will promote employment generation by absorbing the relatively economical, particularly skilled labour force.

   Thus, foreign capital and technology can play a crucial role in the economic development of India.

FOREIGN INVESTMENT POLICY IN INDIA

The Industrial Policy of 1991 made a radical departure from the past and heralded a new era for foreign investment in India. Therefore, India's foreign investment policy can be broadly classified under two periods:

I. **1948 - 1990:** The period which was by and large, characterized by restrictive policies and regulated inflow of foreign capital and technology.

II. **1991 onwards:** The period which has been characterized by remarkable liberalization of foreign investment laws and heartening upswing in foreign investment inflows.

FOREIGN INVESTMENT POLICY; 1948-1990

The Industrial Policy Resolution (IPR) of 1948 was the first organised attempt by the Government of India to give proper direction to the industrialisation process of the economy. IPR, 1948 fully recognised that the participation of foreign capital and enterprise, particularly as regards industrial technique and knowledge, would be of value to the rapid industrialisation of the country. However, the policy stressed the need to properly regulate foreign capital in the national interest. The policy made it clear that, as a rule, the major interest in ownership and effective control should always be in Indian hands. IPR, 1948 emphasized that a suitable legislation is necessary for foreign capital.[34]

Subsequently, the then Prime Minister of India made a statement in the constituent" Assembly in April 1949 on foreign investment which brought out three major issues;

1. India would not make any discrimination between foreign and local enterprises.
2. Foreign investors would be allowed remittance of profits and repatriation of capital if the foreign exchange position permits.
3. If nationalization of a foreign enterprise becomes inevitable, fair and equitable compensation would be given to foreign investors.

Since then, the Government has adhered to this policy statement for almost two decades. Foreign collaborations were encouraged in those industries:

- which were considered essential for the country's development
- which required large capital investments and complex production processes, and
- which helped to produce import substituting and export oriented products, etc.

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[34] *Ibid 28*

In 1968, procedures relating to foreign investments were streamlined. In order to minimize the delays in processing the applications for foreign collaboration, the Government set up a Foreign Investment Board in December 1968. The Board was empowered to deal with all matters relating to private foreign investment and collaboration where foreign investment does not exceed; (1) Rs. 2 Crore of equity capital, and (2) 40 percent of the issued capital. In India private foreign investment have been prominent. [35]

In January 1969, the Government of India came out with an illustrative list of industries where:

a) foreign investment might be permitted
b) only foreign technical collaboration might be permitted but not foreign investment
c) no foreign collaboration (financial or technical) was considered necessary.

In the first two categories, a permissible range of royalty payments was also specified for different items which generally did not exceed 5 percent. The permitted duration of collaborations was reduced from 10 to 5 years and their renewals restricted.

[35] *See, Foreign Capital and Collaborations available at iocg.ignou.ac.in/wiki/images/a/a0/MITI-024-B-4-Unit-16.pdf, last visited on 20/11/09*

Foreign collaboration for industries not included in any of the three lists was left for consideration on merit. These lists were revised a number of times towards narrowing down the area for foreign collaborations. In 1973, the area where foreign investment was permitted was confined to 19 industries.

The Industrial Policy statement of 1973 sought to further restrict the activities of foreign companies to a select*group of core industries. These industries were considered to be of 'basic, critical and of strategic importance'. This was followed by the enactment of the Foreign Exchange Regulation Act (1973) FERA, which influenced the operations of foreign firms more than any other policy statement. FERA became the cornerstone of the regulatory framework for foreign investment in the subsequent years. [36]

In 1948, the stock of foreign investment in India stood at Rs. 256 crore and was mostly from the U.K. A greater proportion of this foreign investment was concentrated in export-oriented raw materials, extractive and service sectors. Tea plantations and jute accounted for more than 25 percent of the total foreign investment; about 32 percent in trading and other services, 9 percent in petroleum and only about 20 percent in manufacturing (excluding jute). By 1990, the stock of foreign investment

[36] *Ibid 35*

has increased by more than ten times, to Rs. 2705 crore. During this period, not only the magnitude but the sect oral composition as well as the sources of foreign investment have undergone considerable changes.

The most significant trend in the increasing size of foreign investment was the growing importance of the manufacturing sector. In 1964, the manufacturing sector had about 40 percent of the stock of foreign investment as compared to less than a quarter in 1948. In 1980, the manufacturing sector accounted for more than three quarters of the stock of foreign investment.

This remarkable increase in the share of the manufacturing sector occurred at the cost of petroleum, plantations and services. Even during the 70s, when the total stock of foreign investment in India stagnated, the sharp of the manufacturing-sector steadily went up. This was largely due to the selective policy of the Government: [37]

- Government of India nationalized foreign concerns in banking, insurance and petroleum sectors.
- In plantations, under FERA, 1973, branches of foreign enterprises were forcibly Indianised (by reducing the foreign equity to 40 percent).

[37] *Ibid 35*

- Foreign investment in the manufacturing sector, particularly in the core sector was welcomed. [38]

In the '80s, however, there was a marginal improvement in the share of plantations and services.

Within the manufacturing sector, new investments were directed at technology intensive sectors such as electrical goods, transport equipment, machinery and machine tools, and chemicals and allied products. These four sectors together accounted for about 74 percent of the stock-of foreign investment in 1990 as compared to about 47 percent in 1964, about 56 percent in 1974 and about 64 percent in 1980. In other words, the relative share of these four sectors in total foreign investment steadily went up. Consequently, the share of traditional industries such as food and beverages, textile products, metal and metal products in foreign investment declined, particularly till the late 70s. The liberalization of foreign investment policies in the '80s, however, arrested and to some extent reversed the declining trend of relative share of foreign investment in consumer goods industries.

There has been geographical diversification in the sources of foreign investment in India. At the time of Independence and almost for the subsequent two to three decades the bulk of foreign investment originated from U.K. In 1964, more than three quarters of the foreign investment in India

[38] *Ibid 35*

were from U.K. (Table 16.2). Another significant contribution came from the U.S.A. whereas other industrialized countries had only a negligible presence. By 1980, the relative share of U.K. declined to about 54 percent whereas the shares of U.S.A., Germany, Sweden, Canada and Switzerland increased significantly. By 1990, though still the most prominent source of foreign investment, the share of U.K. in foreign investment in India had fallen below the one-half mark and Germany, Japan and other industrialized countries had emerged as the other prominent sources of foreign investment for India.

The introduction of the new industrial policy in 1991 to facilitate the Indian economy in general, and industry in particular to achieve international competitiveness, led to the implementation of radical changes in India's foreign investment policy. The policy duly recognized the role and importance of foreign capital and technology in the industrial development of India.

To provide a large role for foreign investment and technology, the Foreign Exchange Regulation (Amendment) Act, 1993 was brought into force. As of now, India welcomes foreign investment and technology virtually in every sector of the economy except those of strategic concern such as defense, railways and atomic energy. Foreign investment need not necessarily be accompanied by foreign technology.

In the '90s there has been much more geographical diversification as far as the origin of foreign investment is concerned. Though the U.S. is the major source of foreign investment, many more industrialized as well as industrializing countries are increasingly turning towards India for investment. Today India attracts foreign investments from as many as 80 countries across the world. These include countries from America, Europe, Middle East, Africa, Australia and different parts of Asia. Thus, India has been experiencing a significant increase in the magnitude, wider dispersion in terms of origin and direction of foreign investment in the '90s.

The trend in the actual inflow of foreign direct investment is a more clear reflection on the Government's foreign investment policy. Even the actual inflow of foreign direct investment has steadily gone up in the 90s.

All these bring out clearly the fact that the liberalization of India's foreign investment policy has had a major impact on foreign investment and collaborations. The recognition of the role of foreign investment in economic development by India and the recognition of India as an important investment destination by foreign investors will have a long lasting impact on the globalization process of the Indian economy.

India's foreign investment policy has come a long way since independence. Though foreign investment and technology was welcomed initially, the subsequent strain on the foreign exchange reserves due to dividend repatriation, royalty payments etc. and complaints of repetitive import of same technology prompted the Government to go for a selective and restricted approach. But the failure of the Indian industry to develop technology on its own and the consequent decline of competitiveness, made the Government to liberalize the foreign investment policy. But these policy changes during 1948-1990 did not make any major and significant dents on the trend of foreign investment and collaborations. FERA continued to be a major deterrent for foreign investment.

It is in the '90s mat the Government has gone for an overhaul of foreign investment policy. FERA 1973 has been diluted largely and foreign investment is welcomed in a wide range of sectors. Foreign investors have responded positively to India's policy changes. There has been a gradual and steady increase in both foreign investment and technical collaborations — approvals as well as actual inflow.

The question that has often been asked is — will foreign investment and technology benefit the economy? or will it ruin the economy? Giver the resources and diversified economic structure and strength of India, foreign capital and technology will largely be beneficial to India's industrialization and economic development.

2.5 Foreign Technology Agreements

There is a great need for promoting an industrial environment where the acquisition of technological capability receives priority. In the fast changing world of technology the relationship between the suppliers and users of technology must be a continuous one. Such a relationship becomes difficult to achieve when the approval process includes unnecessary governmental interference on a case to case basis involving endemic delays and fostering uncertainty.

The Indian entrepreneur has now come of age so that he no longer needs such bureaucratic clearances of his commercial technology relationships with foreign technology suppliers. Indian industry can scarcely be competitive with the rest of the world if it is to operate within such a regularity environment. [39]

With a view to injecting the desired level of technological dynamism in Indian industry, Government will provide automatic approval for technology agreements related to high priority industries within specified parameters.

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[39] *Ibid 24*

Similar facilities will be available for other industries as well if such agreements do not require the expenditure of free foreign exchange. Indian companies will be free to negotiate the terms of technology transfer with their foreign counterparts according to their own commercial judgment. The predictability and independence of action that this measure is providing to Indian industry will induce them to develop indigenous competence for the efficient absorption of foreign technology.

Greater competitive pressure will also induce our industry to invest much more in research and development than they have been doing in the past.

In order to help this process, the hiring of foreign technicians, and foreign testing of indigenously developed technologies, will also not require prior clearance as prescribed so far, individually or as a part of industrial or investment approvals. [40]

2.6 Public sector policy

The public sector has been central to our philosophy of development. In the pursuit of our development objectives, public ownership and control in critical sector of the economy have played an important role in preventing the concentration of economic power, reducing regional

[40] *Ibid 24*

disparities and ensuring that planned development serves the common good.

The Industrial Policy Resolution of 1956 gave the public sector a strategic role in the economy. Massive investments have been made over the past four decades to build a public sector, which has a commanding role in the economy. Today key selectors of the economy are dominated by the mature public enterprises that have successfully expanded production, opened up new areas of technology and built up a reserve of technical competence in a number of areas.

After the initial exuberance of the public sector entering new areas of industrial and technical competence, a number of problems have begun to manifest themselves in many of the public enterprises. Serious problems are observed in the insufficient growth in productivity, poor project management, over-manning, lack of continuous technological up gradation and inadequate attention to R&D and human resources development. In addition, public enterprises have shown a very Low rate of return on the capital invested. This has inhibited their ability to regenerate themselves in terms of new investments as well as in technology development.

The result is that many of the public enterprises have become a burden rather than being an asset to the

Government. The original concept of the public sector has also undergone considerable dilution. The most striking example is the takeover of sick units from the private sector. This category of public sector units accounts for almost one third of the total losses of central public enterprises. Another category of public enterprises, which does not fit into the original idea of the public sector being at the commanding heights of the economy, is the plethora of public enterprises which are in the consumer goods and services sectors. [41]

It is time, therefore, that the Government adopts a new approach to public enterprises. There must be a greater commitment to the support of public enterprises, which are essential for the operation of the industrial economy. Measures must be taken to make these enterprises more growth oriented and technically dynamic. Units, which may be faltering at present but are potentially viable must be restructured and given a new lease of Life. The priority areas for growth of public enterprises in the future will be the following:

- Essential infrastructure goods and services
- Exploration and exploitation of oil and mineral resources

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[41] *G. D. Sharma - New India Policy & Relation, Published by Press & Publication Agency, ed 2006*

- Technology development and building of manufacturing capabilities in areas which are crucial in the long term development of the economy and where private sector investment is inadequate
- Manufacture of products where strategic considerations predominate such as defense equipment.
- At the same time the public sector will not be barred from entering areas not specifically reserved for it.

In view of these considerations, Government will review the existing portfolio of public investments with greater realism. This review will be in respect of industries based on low technology, small scale and non-strategic areas, inefficient and unproductive areas, areas with low or nil social considerations or public purpose, and areas where the private sector has developed sufficient expertise and resources. [42]

Government will strengthen those public enterprises, which fall in the reserved areas of operation or are in high priority areas or are generating good or reasonable profits. Such enterprises will be provided a much greater degree of management autonomy through the system of memoranda of understanding. Competition will also be induced in these

[42] *Ibid 41*

areas. Government holdings in the equity share capital of these enterprises will be disinvested in order to provide further market discipline to the performance of public enterprises. There are a large number of chronically sick public enterprises incurring heavy losses, operating in a competitive market and serve little or no public purpose. These need to be attended to. The country must be proud of the public sector that it owns and it must operate in the public interest. [43]

2.7 <u>Monopolies and Restrictive Trade Practices Act (MRTP Act)</u>

The principal objectives sought to be achieved through the MRTP Act are as follows:

i. Prevention of concentration of economic power to the common detriment, control of monopolies, and
ii. Prohibition of monopolistic and restrictive and unfair trade practices.

The MRTP Act became effective in June 1970. With the emphasis placed on productivity in the Sixth Plan, major amendments to the MRTP Act were carried out in 1982 and 1984 in order to remove impediments to industrial growth and expansion. This process of change was given a new

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[43] *Ibid 41*

momentum in 1985 by an increase of threshold limit of assets.

With the growing complexity of industrial structure and the need for achieving economies of scale for ensuring higher productivity and competitive advantage in the international market, the interference of the Government through the MRTP Act in investment decisions of large companies has become deleterious in its effects on Indian industrial growth. The pre-entry scrutiny of investment decisions by so-called MRTF companies will no longer be required. Instead, emphasis will be on controlling and regulating monopolistic, restrictive and unfair trade practices rather than making it necessary for the monopoly houses to obtain prior approval of Central Government for expansion, establishment of new undertakings, merger, amalgamation and takeover and appointment of certain directors.

The thrust of policy will be more on controlling unfair or restrictive business practices. The MRTP Act will be restructured by eliminating the legal requirements for prior governmental approval for expansion of present undertakings and establishment of new undertakings. The provisions relating to merger, amalgamation, and takeover will also be repealed. Similarly, the provisions regarding restrictions on acquisition of and transfer of shares will be appropriately incorporated in the Companies Act. [44]

Simultaneously, provisions of the MRTP Act will be strengthened in order to enable the MRTP Commission to take appropriate action in respect of the monopolistic, restrictive and unfair trade practices. The newly empowered MRTP Commission will be encouraged to require investigation sue mote or on complaints received from individual consumers or classes of consumers.

Decisions of Government

In view of the considerations outlined above, the Government has decided to take a series of measures to unshackle the Indian industrial economy from the cobwebs of unnecessary bureaucratic control. These measures complement the other series of measures being taken by the Government in the areas of trade policy, exchange rate management, fiscal policy, financial sector reform and overall macro economic management.

The salient features of the new industrial policy are summarized as follows:

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[44] *See, Company Law, Published by Avtar Singh, Central Law Agency, ed 2006*

A. Industrial Licensing Policy

i. Industrial Licensing will be abolished for all projects except for a short list of industries related to security and strategic concerns, social reasons, hazardous chemicals and over-riding environmental reasons, and items of elitist. Industries reserved for the small scale sector will continue to be so reserved.

ii. Areas where security and strategic concerns predominate will continue to be reserved for the public sector.

iii. In projects where imported capital goods are required, automatic clearance will be given.

   a. In case where foreign exchange availability is ensured through foreign equity.

   b. If the CIF value of imported capital goods required is less than 25% of total value (net of taxes) of plant and equipment, up to a maximum value of Rs.2 crores. In view of the current difficult foreign exchange situation, this scheme (ex. (iii) b) will come into force from April 1992. In other case, imports of capital goods will require clearance from the Secretariat of Industrial Approvals (SIA) in the Department of Industrial Development according to availability of foreign exchange resources.

iv. In locations other than cities of more than 1 million populations, there will be no requirement of obtaining industrials from the Central Government except for industries subject to compulsory licensing. In respect of cities with population greater then 1 million, industries other than those of a non-polluting nature such as electronics, computer software and printing will be located outside 25 kilometers. Of the periphery, except in prior designated industrial areas.

A flexible location policy would be adopted in respect of such cities (with population greater than 1 million) which require industrial re-generation. Zoning and Land Use Regulation and Environmental legislation will continue to regulate industrial locations.

Appropriate incentives and the design of investments in infrastructure development will be used to promote the dispersal of industry particularly to rural and backward areas and to reduce congestion in cities.

v. The system of phased manufacturing programmes run on an administrative case by case basis will not be applicable to new project. Existing projects with such programmes will continue to be governed by them.

vi. Exiting units will be provided a new broad banding facility to enable them to produce any article without additional investment.

vii. The exemption from licensing will apply to all substantial
expansions of existing units.

viii. The mandatory convertibility clause will no linger be applicable for term loans from the financial institutions for new projects and substantial expansions. [45]

Procedural Consequences

ix. All existing registration schemes (Deli censed Registration, Exempted Industries Registration, and DGTD Registration) will be abolished.

x. Entrepreneurs will henceforth only be required to file an information memorandum on new projects and substantial expansions.

B. Foreign Investment

i. Approval will be given for direct foreign investment up to 51 per cent foreign equity in high priority industries. There shall be no bottlenecks of any kind in the process. Such Clearance will be available if foreign equity covers the foreign exchange requirement for imported capital goods. Consequential amendments to the Foreign Exchange Regulation Act (1973) shall be carried out.

[45] *Ibid 44*

ii. While the import of components, raw materials and intermediate goods, and payment of know how fees and royalties will be governed by the general policy applicable to other domestic units, the payment of dividends would be monitored through the Reserve Bank of India so as to ensure that out flows on accounts of dividend payments are balanced by export earnings over a period of time.

iii. Other foreign equity proposals, including proposals involving 51% foreign equity which do not meet the criteria under (ii) above will continue to need prior clearance. Foreign equity proposals needs not necessarily be accompanied by foreign technology agreements.

iv. To provide access to international markets, majority foreign equity holding up to 51% equity will be allowed for trading companies primarily engaged in export activities. While the thrust would be on export activities, such trading houses shall be at par with domestic trading and export houses in accordance with the Import-Export Policy.

v. A special Empowered Board would be constituted to negotiate with a number of large international fines and approved direct foreign investment in select areas. This would be a special programme to attract substantial investment that would provide access to high technology and world markets. The investment programmes of such firms would be considered in totality, free from pre-determined parameters or procedures.[46]

C. Foreign Technology Agreements

i. Automatic permission will be given for foreign technology agreements in high priority industries up to a lump sum payment of Re. 1 crore 5% royalty for modestic sales and 8% for exports subject to total payments of 8% of sales over a 10 year period from date of agreement or 7 years from commencement of production. The prescribed royalty rates are net of taxes and will be calculated according to standard procedures.

ii. In respect of industries other than those in, automatic permission will be given subject to the same guidelines as above if no free foreign exchange is required for any payments.

iii. All other proposals will need specific approval under the general procedures in force.

iv. No permission will be necessary for hiring of foreign technicians, foreign testing of indigenously developed technologies, Payment may be made form blanket permits or free foreign exchanges according to RBI guidelines.

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[46] *Ibid 44*

D. <u>Public Sector Policy</u>

i. Portfolio of public sector investments will be reviewed with a view to focus the public sector on strategic, high-tech and essential infrastructure. Whereas some reservation for the public sector is being retained there would be no bar for areas of exclusivity to be opened up to the private sector selectively. Similarly the public sector will also be allowed entry in areas not reserved for it.

ii. Public enterprises which are chronically sick and which are unlikely to be turned around will, for the formulation of revival / rehabilitation schemes, be referred to the Board for Industrial and financial Reconstruction (BIFR), or other similar high level institutions created to protect the interests of workers likely to be affected by such rehabilitation packages.

iii. In order to raise resources and encourage wider public participation, a part of the government's shareholding in the public sector would be offered to mutual funds, financial institutions, general public and workers.

iv. Boards of public sector companies would be made more professional and given greater powers.

v. There will be a greater thrust on performance improvement through the Memoranda of Understanding (MOU) system through which management's would be granted greater autonomy and will be held accountable. Technical expertise on the part of the Government would be upgraded to make the MOU negotiations and implementation more effective.

vi. To facilitate in a fuller discussion on performance, the MOU signed between Government and the public enterprise would be placed in Parliament. While focusing on major management issues, this would also help place matters on day to day operations of public enterprises in their correct perspective. [47]

E. MRTP Act

The MRTP Act will be amended to remove the threshold limits of assets in respect of MRTP companies and dominant undertakings. This eliminates the requirement of prior approval of Central Government for establishment of new undertakings, expansion of undertakings, merger, amalgamation and takeover and appointment of Directors under certain circumstances.

i. Emphasis will be placed on controlling and regulating monopolistic restrictive and unfair trade practices. Simultaneously, the newly empowered MRTP Commission will be authorized to initiate investigations sue motto or on complaints received from individual consumers or classes of consumers in

[47] *Ibid 44*

regard to monopolistic, restrictive and unfair trade practices.

Necessary comprehensive amendments will be made in the MRTP Act in this regard and for enabling the MRTP Commission to exercise punitive and compensatory powers.