Monthly Economic Report December 2014 – Reform Update

British High Commission New Delhi

Summary

- Reforms in insurance, mining, land acquisition and arbitration passed through executive ordinance post Winter Parliamentary session.
- Successor to Planning Commission confirmed (special note)

Winter Parliamentary session

A number of key economic legislations remained stalled in the Winter Parliamentary session in the Upper House. Ultimately the government went through the 'ordinance route', with insurance, mining, land acquisition, and corporate arbitration reforms confirmed by executive order. **The ordinances need to be ratified by the Parliament in the next (Budget) session, or they will lapse.**

A round up of the latest status of key economic legislations:

GST: India is not a unified market, and disparate state tax policies can feel like trading between different countries. To implement the proposed unified sales tax, GST (Goods and Sales Tax), the Constitution first needs to be modified to dissolve the centre-state separation of tax jurisdiction. Approval is needed from both Houses of Parliament and at least 15 state legislatures with a two-thirds majority. Then a GST bill has to be passed by the Parliament and state legislatures. As of now although states have not agreed to include alcohol in GST (this is an important source of income for many states); they have agreed on including petroleum products (important or else an important part of the value chain will be out of the common tax regime). The centre has also promised to compensate states for revenue loss for the first five years. Armed with this consensus, the government tabled the bill in the Lok Sabha. This needs to be ratified in the next Parliamentary session to meet the April 2016 deadline for GST rollout.

The Planning Commission is now NITI Aayog

NITI stands for 'National Institution for Transforming India'. The overarching economic advisory body will be headed formally by the PM, and chaired by ex-Columbia economist Arvind Panagariya. The team comprises Bibek Debroy (another noted economist), a handful of Cabinet ministers, a former chief of the government defence research organisation, and a bureaucrat as CEO.

Why the change? The Planning Commission was an inheritance of Soviet style central planning. Its role became increasingly muddled over the years – from determining the inter-state allocation of central funds, to drafting model PPP contracts, to running complex economic models, to micro-managing social sector schemes. It was criticised for being unrepresentative of states' interests.

What has changed? So far, two key aspects (a) the new body will not allocate resources, instead being limited to a think tank; (b) states will be equal partners, in the spirit of cooperative federalism.

Part of a bigger plan? A renovated NITI Aayog is part of the wider policy constellation the government is putting in place. The Department of Industrial Policy & Promotion, within the Ministry of Commerce, has been made the nodal agency to exhort states to improve ease of doing business and 'Make in India'. This, along with the government's efforts to increase efficiency of the bureaucracy, shows the government's vision beyond legislation.

Mining: traditionally coal blocks were allocated to 'priority' industries without any form of auction. Recently, in the wake of cancellations of coal block allocations by the Supreme Court, the government introduced new ordinances on coal and other mining industries seek to establish an auction based system. This is also expected to enventually lead to commercial mining of coal, breaking what has been so far a state monopoly, through Coal India. Employees of Coal India announced a five day strike but this was called off after negotiations with the coal minister.

Land acquisition: the previous government put forward legislation that required 70% of land owners to consent pre-acquisition, causing bottlenecks for new investment projects. The new ordinance reduces the assent required

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to 50% for PPP projects and none for government projects. The required social impact assessment has also been diluted in order to reduce the indirect costs imposed on business.

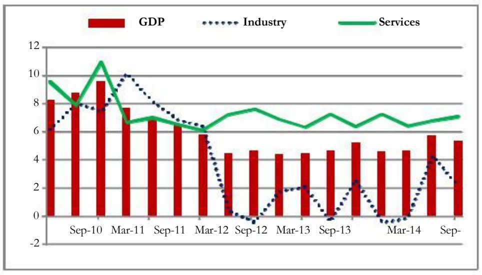
Insurance: the potential market is huge – estimates are that the present $66 bn market will grow to $350-400 bn by 2020. The move to increase FDI from 26% to 49% was originally a 2004 BJP idea, and the previous Congress government could not clear it through its decade long term. Following the ordinance, British insurer Bupa has announced its intention to raise its stake in its Indian joint venture to 49%.

Arbitration: one of the major hurdles for both foreign and Indian corporates in India are the time-consuming arbitration and dispute resolution processes. It is now mandatory for commercial disputes to be settled within nine months and arbitrator's fees to be capped. There is talk of dedicated fast-track courts for dealing with arbitration cases. The government has inherited almost 17 MNCs in international arbitration disputes over policy reversals which have hurt their investments.

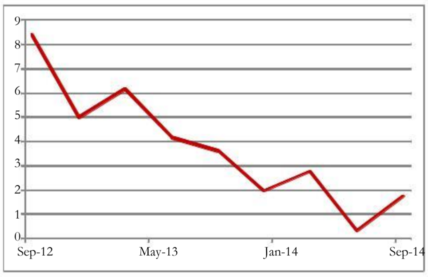
We also publish a monthly trade report. Our previous reports are accessible here.

GROWTH: *Uptick in projects under implementation*

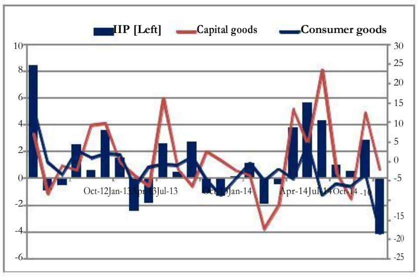
GDP



Projects Under Implementation

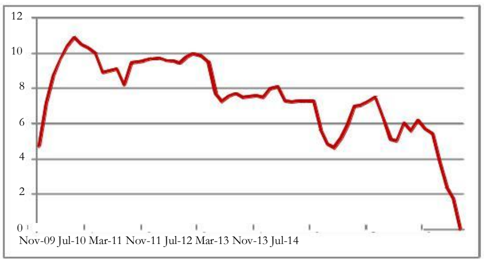


IIP/Capital/Consumer Goods

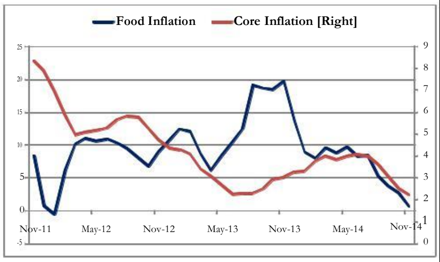


INFLATION: *WPI inflation dips to 0% in November 2014*

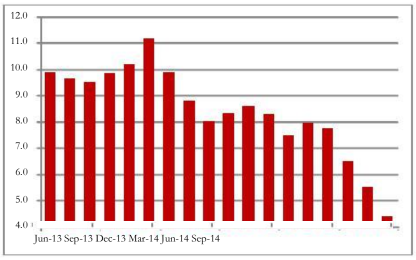
Wholesale Price Index (% y/y)



Food vs. Core Inflation (% y/y)

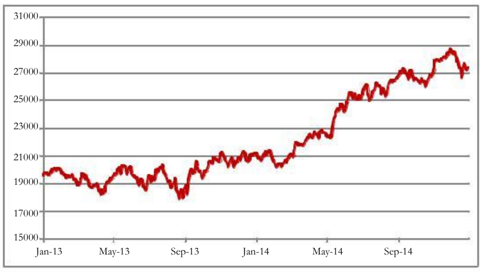


Consumer Price Index (% y/y)

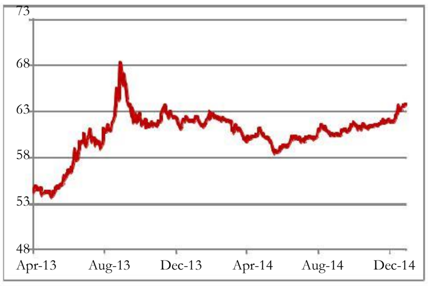


MARKETS: *Some weakness observed in currency markets*

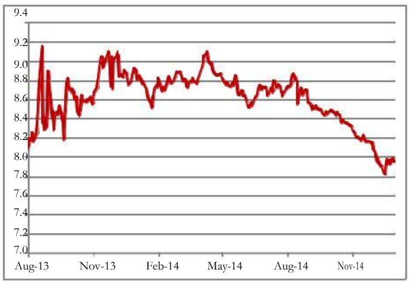
SENSEX



USD/INR

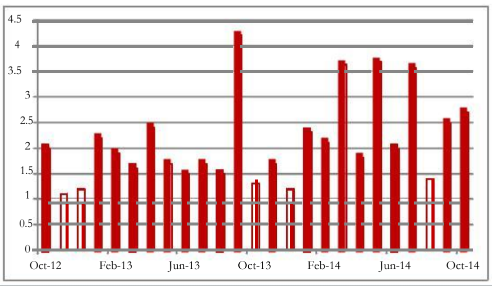


10yr Govt. Securities yield (%)

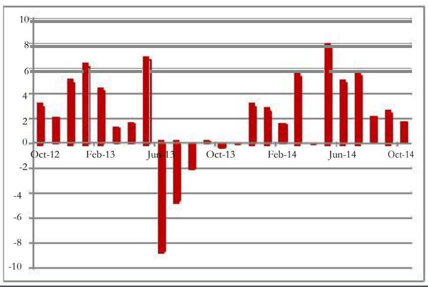


EXTERNAL: *Gold import surge pushed current account deficit to $10.1 bn in Q2 FY 2014-15*

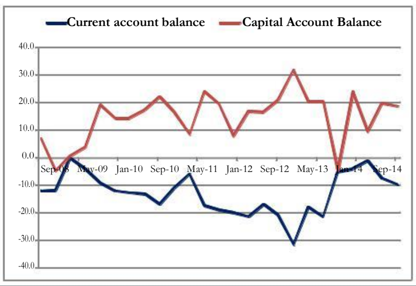
FDI ($ Bn)



FII ($ Bn)

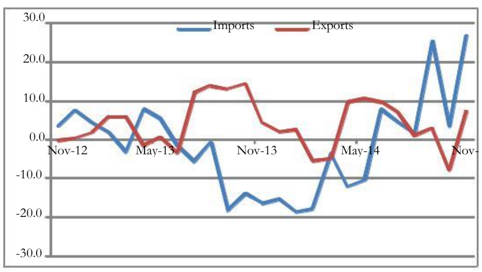


Current vs. Capital A/c ($ Bn)

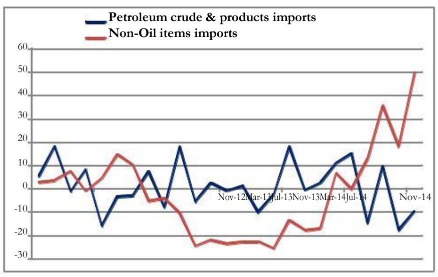


TRADE: *Despite exports being up by 7.3%, trade deficit widens to 18-months high in November 2014*

Export/Import Growth (% y/y)



Imports- Oil and Non Oil (% y/y)



Trade Balance ($ Bn)