

# NEWSLETTER

INSTITUTE FOR STUDIES IN INDUSTRIAL DEVELOPMENT

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## ISID FOUNDATION DAY

*May 01, 2010*

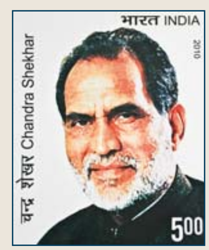
*Prof. S.K. Goyal, Vice-Chairman ISID, speaks on the occassion of the institute's Foundation Day*

Twenty Fourth Foundation Day of ISID was celebrated on May 01, 2010. Prof. T.P. Bhat made introductory remarks while Prof. S.K. Goyal, Vice-Chairman, inaugurated the celebrations. Briefly explaining about the history and vision of the Institute, Prof. Goyal in his inaugural speech, identified a number of new areas of research to be undertaken at the Institute. He stressed the need to undertake meaningful policy oriented research in areas of social relevance and concern, like health, education, etc. Prof. Goyal felt that ISID could come to be seen as a lobbyist for progressive socio-economic development that would engage policy makers in meaningful dialogue and debate. He emphasised and encouraged aggressive use of new technology and media for reaching out to policy makers, academics and administrators.

On this occasion, Prof. Surajit Mazumdar, ISID Faculty Member, made a presentation on the "Current Account Balances, Investment and Growth in Developing Countries: The Odd Case of India". Prof. Mazumdar's presentation was based on work in progress analysing the trends and tendencies of the Indian economy taking into account what is happening in the global economy more explicitly than has been generally the case. It brings together three themes that have been the subjects of recent discussions, but separately from each other. The first of these is the peculiar feature of the world economy since the late 1990s that has been called the 'capital flows paradox' or the phenomenon of 'capital flowing uphill'. The second is the transition experienced by the Indian economy in the early years of the current century when the growth rates of her aggregate GDP, till the global crisis caused an interruption, moved to levels unprecedented in her history. The likelihood of the Indian economy reverting to that growth trajectory in the post-global crisis context is the final issue that he discussed in conjunction with the other two.

Full lecture of Prof. Mazumdar, based on this presentation, is covered in this issue under the heading 'Observation' (Pp. 9–11).

## Postal Stamp in Honour of Late Shri Chandra Shekhar




Shri M. Hamid Ansari, Honorable Vice-President of India released a Commemorative Five-rupee Postal Stamp in Hounour of Late Shri Chandra Shekhar, former Prime Minister and Chairman ISID, on his 84th birth anniversary on April 17, 2010 at Vigyan Bhawan, New Delhi.

## ICSSR National Fellowship to Prof. Sunanda Sen

Indian Council of Social Science Research (ICSSR) awarded National Fellowship to Prof. Sunanda Sen, *Visiting Professor* at ISID, for her outstanding contribution to the field of social sciences, to work on "Globalization, the Development Question and the Current Crisis of Capitalism: A Study of India and China". Prof. Sunanda Sen is going to undertake her research from ISID.

ISID

## SYMPOSIUM

# CONCEPTS, DEFINITIONS AND DATA ISSUES RELATING TO FDI IN INDIA

*March 16, 2010*

Many years after India liberalised her inward foreign direct investment (FDI) regime in 1991, after much concern, discussion and investigation over the low level of inflows, further opening up of individual sectors and FDI limits and attempting to improve investment procedures, official data on FDI inflows registered sudden and sharp increase after 2005–06. This increase came much later than the change in the pattern of reporting the inflows data to meet the international best standards by including additional items under FDI. Occasional doubts could, however, be heard about the composition of the increased inflows. On the other side, while India liberalised her FDI regime substantially, it retained restrictions on FDI in a few sectors on considerations such as national security and sensitivities. Keeping in view occasional attempts at breaching these restrictions, to consolidate the various press notes issued over a period of time and to provide the investors a clear and concise picture of the policy and procedures relating to FDI, the government released a Draft Press Note "FDI Regulatory Framework" on December 24, 2009 for public comments. Taking advantage of the past and ongoing work on FDI at the institute, the ISID contributed to the policy debate by organising a Symposium Concepts, Definitions and Data Issues Relating to FDI in India in association with the Research and Information System for Developing Countries (RIS) on March 16, 2010.

The proceedings were initiated by Prof. S.R. Hashim, Director ISID, who, after welcoming the participants, briefly explained the context in which the Symposium was being organised. Prof. S.K. Goyal, Vice-Chairman ISID, who presided over the occasion, recounted the strong base developed by the Institute from the days of the Corporate Studies Group (CSG) and how it came to be acknowledged for its studies on multinational corporations. He also underlined the need to continue the type of studies initiated at the CSG and to establish the interface between FDI and Indian large business houses. Prof. Sunanda Sen, ICSSR National Fellow (ISID) chaired the Symposium and conducted the proceedings. She underlined the importance of the subject and also spoke about the two organising institutions. The symposium was well attended with participants from academics, research scholars, RBI and other official agencies, independent analysts, and journalists making valuable contributions.

The background paper for the Symposium "Accelerating India's FDI Inflows & Conceptual and Definitional Issues" was prepared jointly by Prof. K.S. Chalapati Rao of ISID and Prof. Biswajit Dhar of RIS. Based on an analysis of the officially reported actual individual inflow records during September 2004 to December 2008, each amounting to a minimum of $5 million, the paper raised a number of issues and sought to dispel the general impressions surrounding FDI in general and of that in India, in particular. The paper underlined the ambiguities in measuring FDI, especially the choice of 10 per cent as being sufficient condition to represent control and lasting interest and hence as the benchmark for indentifying an FDI relationship. In the process it discussed at length the issue of corporate control. The second main point raised in the paper was with regard to the classification of certain category of investors. The third one related to the extent of adherence to the accepted international norms by Indian official agencies. It also raised the possibility of reported acquisition of shares underestimating the extent of takeover of Indian businesses by foreign companies. The paper also tried to address the issue of indirect FDI and the operation of sectoral limits.

While some of the foreign investments would qualify as FDI mainly because the foreign equity constitutes 10 per cent or more of the investee company's equity capital, these generally lack the other essential qualities associated with FDI as a bundle of capital, technology, access to international marketing network, specialised skills, management techniques, etc., which are the chief attractions for the developing countries to liberalise their foreign investment regimes. Investments by private equity investors, venture capitalists and hedge funds which together constituted almost 27 per cent of the total inflows studied are more akin to portfolio investments devoid of most characteristics of the bundle. Leaving aside these investments and investments by banks and investments controlled by Indians themselves, etc., what qualifies to be FDI works out to a little less than half of the total reported inflows. The 10 per cent limit came to be accepted as the international norm due to the coordinated attempts by international agencies mainly to achieve international comparability. It has also been noted that in the manufacturing sector for which many of the traditional expectations from FDI are relevant, accounts for only about one-fifth of the total reported inflows. A good part of the investments by what one would not like to classify as FDI were directed at speculative sectors like construction and real estate. These also happened to be using tax havens to a greater extent for entry into India compared to investments into other sectors and other type of investors.


*Prof. Sunanda Sen, ICSSR National Fellow (ISID), chairs and conducts the proceedings of the symposium*

The others who made special presentations include Prof. C.P. Chandrasekhar of Jawaharlal Nehru University; Dr Sutanu Sinha, Director (Academics), Institute of Company Secretaries of India; Mr Reji K. Joseph of RIS; Shri A.P. Gaur, Advisor, Department of Statistics and Information Management, RBI; Shri Nilmadhab Mohanty, IAS (Retd.), ISID; Ms Premila Nazareth, independent consultant; and Shri Javid Chowdhry, Former Revenue Secretary, Government of India. Prof. Chandrasekhar, while underlining the possibility of control being exercised not merely through equity, but also through technology licensing agreements, explained that the overriding objective of the pre-1990s regime was to encourage domestic participation so as to enable technology transfer to domestic entrepreneurs. In the new regime the expectation from FDI was, similar to the experience of second-tier industrialising countries, that India would be able to attract foreign investors who would make India as a manufacturing base for supply to world markets. He made an important observation which also explains the phenomenon highlighted by the background paper that speculative capital which otherwise could not enter through the FII route (in which case it could have been categorised as portfolio investment) is taking advantage of the liberal FDI policy regime and entering as FDI to avoid scrutiny/restrictions applicable to FII investments. Such hot money flows would obviously not meet the objective of promoting India as a base for production to cater to the world markets. Mr Joseph, while making the presentation 'Analysis of the Performance of FDI Companies in the Drugs and Pharmaceuticals Sector of India' underlined that liberalization of FDI in drugs and pharmaceuticals has not benefited the country in terms of investments in production and R&D. Instead, FDI companies were increasingly becoming trading agents, which procure products locally and sell the same under their own brand names. Ms Satyanand highlighted a number of problems regarding India's FDI statistics and expressed the desire that India would soon be able to bring out data in a format which enables, just by a click of the button, users to get the required information without running to different organisations and yet not finding the required information. Shri Mohanty explained the difficulties associated with administering sectoral caps and called for a transparent and user-friendly FDI policy. He suggested that there should be a clear-cut negative list where FDI was prohibited completely. He was of the opinion that there was no guarantee that the Indian entrepreneurs, who work for their own profit, would be interested in safeguarding national interest and for that there should be appropriate regulatory mechanisms.

Overall, there was the recognition that a clear distinction between different types of foreign investors needs to be made so as to enable proper analysis of their developmental impact. In the absence of such data and analysis, success of the FDI policy would only be measured in terms of attracting larger and larger amount of inflows—an approach which is obviously quite flawed. There is also the need to develop new data sources and improve the existing ones. Multiple official agencies like RBI, Ministry of Commerce & Industry, Ministry of Finance, FIIA, FIPB, SEBI, Planning Commission, Investment Commission, Competition Commission, industry bodies, etc., together with the Ministry of Corporate Affairs should work together to develop such systems. The special dispensation extended to investments from tax havens should be reviewed not only because these are being taken advantage of by speculators and even by domestic entrepreneurs through round-tripping, but also because the benefits from FDI are never automatic.

The symposium concluded with Prof. M.R. Murthy, Joint-Director ISID, proposing the vote of thanks.

## FORTHCOMING EVENTS

### Training Programme on Indian Corporate Sector for Young Economists

*September 27 to October 09, 2010*

The Institute for Studies in Industrial Development (ISID) is organising a two-week Training Programme on the Indian Corporate Sector during September 27 to October 09, 2010. The course is being conducted in the context of increasing use of company level data by economists for analytical purposes and the need to improve their understanding of the Indian corporate sector, various concepts involved, limitations of the reported data, further avenues for research thrown open by the enhanced disclosure requirements for stock exchange listed companies, etc. Broad elements of the programme are: (i) the institution of Joint-Stock Company; (ii) Corporate Sector in India; (iii) Corporate Finance; (iii) Foreign Investments; (iv) Corporate Restructuring; (v) Competition; and (vi) Corporate Disclosures & Databases. The course is sponsored by the Indian Council of Social Science Research (ICSSR), New Delhi.

Young researchers/teachers in academic institutions, colleges and university departments who are primarily from the economics discipline and whose work is related to the Indian corporate sector form the target group for the programme. The batch will consist of 25 participants and selection will be based on relevance of the topic under research/proposed to be taken up. A nominal fee would be charged from the participants @ ₹ 800/- for lecturer or equivalent; @ ₹ 400/- for scholars getting fellowship; and @ ₹ 200/- for those without any fellowship or financial support. The selected scholars will be paid to and fro II class railway fare from the place of study/work. For outstation participants there is provision for boarding and lodging in Delhi for the duration of the programme.

Those desirous of participating in the programme may kindly send their brief CV along with a write-up of around 1,000 words on their research topic so as to reach the Programme Coordinator, preferably through email at corprog@isid.org.in, before August 16, 2010. Further details and programme updates are regularly posted at: http://isid.org.in/corprog.html.

### International Seminar on The Globalization of Production Models and Innovation in Emerging Economies: Comparative Research on Sub-national Industrial Policies

*November 19–20, 2010*

The motivation for organising this seminar is to bring together scholars examining research themes pertaining to the evolution of production models in regions of India and China, in relation to the progressive opening of these large economies to trade and FDI. Of particular interest is a focus on industrial policies emerging at the state or provincial level, presumably more responsive to territorially embedded production systems, which are often specialized in particular sectors and rely on specific types of social capital (assets/liabilities). Equally important is the manner in which these public policies interact with firm-level strategies, to complement or compensate, in pursuit of more broad-based development goals. This reflection, from a subnational perspective, builds on research-in-progress on the industrial policies of several Indian states (Andhra Pradesh, Haryana, Kerala, Tamil Nadu), and on industrial restructuring and technological upgrading in the provinces of Guangdong, Hubei (around the city of Wuhan) and in the Yangtze delta, mainly in textiles, automobiles and IT.

On the basis of this ongoing research, it was observed that there are striking similarities in the constraints and opportunities facing India and China in the context of increasing competition in export markets. Especially remarkable is the expression of identical policy objectives, both national and regional, in both countries concerning industrial development: promoting sectors with higher value added, technological upgrading, and various efforts to generate local employment. At the same time, this research as well as the academic literature published in the field of economic and technological growth in emerging economies stress important differences in the way subnational regions in each country respond to and articulate with global markets. Regional capacities and modes of global articulation remain intimately linked with the specific historical trajectories of industrialization in the concerned regions (past industrial policies, policy environment for foreign investment and trade, political and social factors, to name just a few).

The following considerations are of particular interest:

- the industrial policies emerging at the state or provincial level, which often reflect regional specialisations relying on specific types of social capital;
- the manner in which these public policies interact with firm-level strategies, to complement or compensate, in pursuit of more broad-based development goals;
- technological changes that have occurred as a result of these industrial policies;
- impacts of these policies and related technological changes on employment;
- political implications of the above, in the context of the federal or unitary structures of governance in place.

To explore these themes, the ISID is organising a seminar in Delhi on November 19–20, 2010, in collaboration with two French research institutes, the Centre for Research on Contemporary China (CEFC) in Hong Kong and the Centre for Human Sciences (CSH) in Delhi. This seminar has three main objectives:

- to bring together Indian and Chinese researchers working on these themes, as well as a few invited academics from other emerging economies. This first meeting would allow the coordinators to identify the main similarities and differences in the industrial trajectories of the study regions in terms of policy, restructuring, technological upgrading, and international trade;
- to fill the gap in comparative research in this area by encouraging scholarship in the form of seminar presentations, and by publishing selected papers. This seminar could contribute to stimulating future research in this field;
- to put in place a research network, that could form the basis for a grant proposal to fund subsequent research in India and China is this emerging field.

## RESEARCH PROJECTS

### Completed

- *Industrial Development Process in Contemporary China and India: A Comparative Study*—a collaborative research study of ISID and Institute of Developing Economies (IDE-JETRO), Japan.
- *Aid Salary Discrepancies and Development Workers Performance*—a research project in collaboration with Massey University, New Zealand.
- *SME Clusters in India: Identifying Areas of Intervention for Inclusive Growth*—a research report submitted to the Planning Commission. Prof. S.R. Hashim was the Project Director, Dr Satyaki Roy and Prof. M.R. Murthy are principal researchers.

### Ongoing

- *Structural Changes in Industry and Employment in the Indian Economy: Macro-economic Implications of Emerging Pattern*—a research programme funded by ICSSR.
- *Quality in School Education: Accreditation Standards for MCD Schools for Quality School Governance*—funded by Quality Council of India (QCI), Department of Industrial Development and Policy, Ministry of Commerce & Industry, Government of India.
- *Sustainable Development: Emerging Issues in Indian Mineral Sector*—to analyze as to why in India the mining industry's "social license to operate" is increasingly under threat and what can be done to integrate mineral development with social concerns, environmental integrity and good governance in the mining areas. Research proposal submitted to the Planning Commission.
- ISID, being the host institution for *India Water Partnership (IWP)*, has been facilitating and providing support for its various activities. IWP is presently working on different aspects related to water such as—(i) promoting water as key part of sustainable national development in Uttar Pradesh and Bundelkhand, and Rajasthan; (ii) coping with critical water challenges through partnerships to secure mutual goals; (iii) reinforcing knowledge sharing and communications; and (iv) building more effective linkages of GWP-India with other Networks.

## New Initiatives

- *Determinants and Impact of FDI in R&D in the Creation and Diffusion of Knowledge in the Automobile Industry: A Study on Clusters in Bangalore, Chennai and National Capital Region*—The study is sponsored by Technology Information, Forecasting and Assessment Council (TIFAC), Department of Science and Technology, Government of India.
- *The Employment Implications of Current Financial Crisis: Challenges, Threats and Coping Strategies in India*—After the global slow-down in late 2008 there has been a growing concern over its impact on employment. The study, commissioned by the South Asian Network of Economic Research Institutes (SANEI), aims to analyse the employment impact of recent global slow-down, with special focus on small manufacturing (exporting and non-exporting) enterprises.
- *Employment Challenges in North-Eastern States of India: Role and Potential of the Unorganised Manufacturing Sector*—Based primarily on secondary data sources such as the NSS reports on unorganized manufacturing sector, this study analyses the critical issues of employment challenges and potential in eight north-eastern states of India. The study is supported by the V.V. Giri National Labour Institute, Noida.

# FACULTY NEWS

## Working Papers

**WP2009/02: Footwear Cluster in Kolkata: A Case of Self-exploitative Fragmentation, Satyaki Roy, December 2009.**

Studies in industrial clusters largely identify the institutional failures and deficits that prevail in the supply of indivisible inputs and collective action. This paper critically reviews a typical 'low-road' cluster in Kolkata and argues that market failures due to existence of information imperfections, externalities and public good and the institutional failure to resolve those imperfections only partially explain the depressed status in these clusters. The explanation, however, critically rests on the recognition of the fact of asymmetric power relations and conflicts arising between the trader and the small producer. These give rise to definite types of production relations that thwart the high road growth path. The spawning of small enterprises in such clusters, as the argument goes, is a result of self-exploitative fragmentation that does not flow from a rise in entrepreneurship but is a result of survival strategy of labour in the context of depressed wages

**WP2010/01: Does the Current Global Crisis remind us of the Great Depression? Sunanda Sen, January 2010.**

One identifies strong parallels between what happened during the Great Depression of the 1930s and what the world is passing through this day. While the build up of the crisis shared a similar pattern, subject to payments imbalances and capital flows directed to channels which failed to contribute to real growth in the capital importing debtor nations, official policies as precipitated the crisis also were similar. These included Britain's move to re-incarnate pre-war gold standard in 1925 with overvalued gold parity for Pound Sterling and a dear money policy, both to attract funds from abroad none of which finally worked. In US, free use was made of funds to stimulate the country's stock market transactions with a boom which finally came to an end in October 1929. Likewise, Alan Greenspan's strategy of high interest rate and overvalued dollar during the years preceeding the financial crash in 2008 certainly worked as factors precipitating the collapse. Notwithstanding the acceptance of Keynesianism in post-war Europe, policymakers swung back by mid seventies to pre-Keynesian neo-liberal ideas of monetarist variety. The unprecedented boom in stock markets, with leveraged finance supporting the securitized assets, and the continuing flows of capital to finance the trade and fiscal deficits of US had to give way to unfulfilled expectations in the market. Again, as for reactions, the protectionist wave has re-emerged in Europe and USA, with economic nationalism ruling over notions of multilateralism and free trade. Racial discrimination which led to fascist upheavals during the thirties today remain much camouflaged, garbed in the language of economic nationalism. As for the magnitude of the loss in terms of output and employment, the current scene certainly overtakes the thirties in terms of absolute magnitudes. One only hopes that duration of the slump will not be as long as it happened earlier and also that the world will witness the revival of progressive new ideas, as it happened with the Keynesian revolution in the 1930s!

**WP2010/02: Industry and Services in Growth and Structural Change in India: Some Unexplored Features, Surajit Mazumdar, January 2010.**

This paper briefly presents an analytical description of the twin processes of growth of output and change in its composition in the Indian economy since independence, by looking at the time-paths of the two dimensions simultaneously. It suggests that three turning points located respectively in the mid-1960s, 1980, and the mid-1990s separate the entire period after independence into four sequential phases of growth and structural change. This periodization of India's post-independence economic history points towards the need to go beyond relating the dynamics of the Indian economy to exclusively the degree to which the prevalent economic policy regime was interventionist or liberal in different periods.

**WP2010/03: Trading in India's Commodity Future Markets, Sunanda Sen and Mahua Paul, February 2010.**

Future trading in agricultural goods, and especially in food items has neither resulted in price discovery nor less of volatility in food prices. We observe the steep increases in spot prices for major food items along with a granger causal link from future to spot prices for commodities on which future data was available. We also have noticed a pattern where investments in stock markets have links with those in the commodity market via portfolio adjustments. Moreover, with the opening of cross-border trade, commodity prices have also been guided by the upward movements in prices in international markets. For India, further opening of the future market in commodities, and especially of food, needs to be dispensed with and be treated with caution, in order not to let speculators have a wider playground to play with.

**WP2010/04: Private Industry and the Second Five Year Plan: The Mundhra Episode as Exemplar of Capitalist Myopia, Nasir Tyabji, May 2010**

In a note to Jawaharlal Nehru in 1958, when it became clear that T.T. Krishnamachari would be forced to resign as Finance Minister in the aftermath of the Mundhra case, M.O. Mathai claimed that he had evidence that it was Krishnamachari's fiscal policies that had led to this denouement. Mathai added that in implementing these policies, Krishnamachari was faithfully operationalising (Nehruvian) socialism. This paper, based on contemporary records, reaches the conclusion that this was, indeed, so. However, the paper argues that more significant than Mundhra in comprehending the reasons for Krishnamachari's fall from grace was the "Rama Rau affair"of late 1956. Often this is trivialised as symbolising the process of destruction of the RBI's proud tradition of autonomy in monetary policy making, or even as an entertaining clash of large individual egos. This paper holds that the government, in formulating procedures to mould monetary policy to the requirements of industrial development through the institutional subordination of the RBI, laid the foundations of an effective industrial policy. Finally, the paper concludes that Krishnamachari tripped in attempting more: he tried to force businessmen in control of industry to behave like true industrialists. In this he provided an object lesson in political economy: the deadly limits to the relative autonomy of the state.

**WP2010/05: Social Science Research in Globalising India: Historical Development and Recent Trends, T.S. Papola, May 2010**

Social science research in India has come under serious criticism in recent years for not having met expectations in terms of analysing some basic structural aspects of the economy and society that have emerged, particularly in the wake of the India's quest for globalisation, meeting some internationally set standards of quality and providing inputs for policy and teaching in higher education. Some of these failures are attributed, for example, by the Fourth Review Committee of the ICSSR, to the increasing trend of lack of resources, commercialisation and privatisation of social science research in recent years. Was social science research meeting these expectations in earlier years? Has there been a qualitative change in the scenario in the recent years? What factors are responsible for this change? What major changes are required to remedy the situation? Are some of the 'reforms' being currently advocated likely to improve the situation? These and related issues are examined in historical and contemporary perspectives in the paper.

## Papers / Articles

- T.S. Papola, "Labour in a Globalized World: Issue of Employment, Labour Standards and Social Protection" in Ranjit Singh Ghuman, Surjit Singh and Jaswinder Singh Brar (eds), *Globalization and Change, Perspectives from Punjab—Essays in Honour of Professor S.S. Gill*, Rawat Publications, Pp. 71–86, 2010.
- Satyaki Roy, "Automobile Industry in India: Emerging Conflicts between Scale and Scope", in Moriki Ohara and Koichiro Kimura (eds), *Industrial Development in China and India: Comparison of the Clusters and Firms*, Institute of Developing Economies (IDE-JETRO), Japan, March 2010.
- P.L. Beena (Co-author), "Exchange Rate and Export Behaviour of Indian Textiles & Clothing Sector: An Enquiry for Major Destination Countries", *CDS Working Paper No. 425*, March 2010.
- T.S. Papola and Alakh N. Sharma, "Globalisation, Work and Social Exclusion in India: Evolving an Inclusionary Policy Framework", in Shashi Moti Lal and Bijayalaxmi Nanda (eds), *Understanding Social Inequality—Concerns of Human Rights, Gender and Environment*, Macmillan, 2010.
- T.P. Bhat and Mahua Paul, "Measurement of Import Intensity of Exports in India", *The Journal of Income and Wealth*, Back Issue, Vol. 31, No. 1, January–June 2009, Pp. 81–92.
- Satyaki Roy reviewed the book, *Imagining Economics Otherwise: Encounters with Identity/Difference* by Nitasha Kaul in *The Book Review*, Vol. 34, No. 3, March 2010, Pp. 21–22.
- T.P. Bhat, "Assessing China's Compliance with WTO Commitments", *India Quarterly*, Back Issue, Vol. 65, No. 3, 2009, Pp. 215–35.

## Presentations / Participants

- Veena Khanduri under the India Water Partnership (IWP) attended a 5-day Regional Conference on "Climate Change & Water Resources: IWRM as a Tool to Cope with Changing Conditions of the Climate Change System" organised by CapNet South Asia Regional Secretariat host institution, Bangladesh Centre for Advanced Studies (BCAS) at Dhaka, Bangladesh, January 10–14, 2010. During the workshop, she chaired a session on the theme "Case Studies: Impacts of Climate Change on Water Use Sector" and also led two group exercises.
- S.R. Hashim was invited to the Finance Minister's Pre-Budget Meeting with Economists, January 15, 2010.
- T.S. Papola participated and chaired a session in International Consultation on *Human Development in India: Emerging Issues and Policy Perspective* organised by IHD, ICSSR and the World Bank, Nehru Memorial Museum and Library, Teen Murti Bhawan, New Delhi, February 05–06, 2010.
- Nasir Tyabji attended the Round Table Conference at IIC, Delhi, February 08, 2010 to discuss the document *Innovation, Sustainability, Development: A New Manifesto* prepared by the STEPS Project Team constituted by IDS, Sussex, and the Science and Technology Policy Research Unit (SPRU).
- T.S. Papola delivered Valedictory Lecture in the course on "Quantitative Methods in Labour Research", at V.V. Giri National Labour Institute, NOIDA, February 19, 2010.


*Prof. S.R. Hashim, Director ISID with Union Finance Minister, Shri Pranab Mukherjee at the Pre-Budget Meeting with Economists, in New Delhi on January 15, 2010*

- Sunanda Sen gave a lecture on "Gendered Aspects of Globalisation" at Hosei University Institute of Sustainable Research and Education, February 25, 2010 at Hosei Univesity, Tokyo.
- T.S. Papola delivered the inaugural address and participated in National Workshop on *Inclusive Innovation Systems and MSME Clusters in Rural India: Possibilities and Challenges*, Gujarat Institute of Development Research, Gota, Ahmedabad, February 27, 2010.
- Sunanda Sen participated in a seminar on "Global Finance" at Economics Department, Hosei University, Tokyo, February 27, 2010.
- P.L. Beena presented a paper on "Merger Waves in India: In Pursuit of an Appropriate Regulatory Regime" in a conference on *Technology, Trade and Development in India*, hosted at GIDR, Ahmedabad in Memory of Prof. K.K. Subrahmanian, February 28, 2010
- Veena Khanduri was invited by Sri Lanka Water Partnership and GWPO, who had organised a three-day "Training Programme on Outcome Mapping" for the Country Coordinators of GWP-SAS, March 01–04, 2010.
- Sunanda Sen presented a paper on "Meltdown of Global Economy: A Keynes-Minsky Episode" at International Keynes Conference in Sophia University, March 02–03, 2010.
- Mahua Paul presented a paper on "Impact of Import Intensity on Export, Output and Employment: An Empirical Analysis" at the Golden Jubilee of Indian Econometric Society Conference, held at Jammu, March 04–06, 2010.
- T.S. Papola delivered Keynote Address on "Global Recession and Indian Economy: Short-term Impact, Medium Term Prospects and Long Term Concerns" at the National Seminar on *Growth Prospects of Indian Economy under Recessionary Conditions*, Meerut College, March 07, 2010.
- Veena Khanduri participated in a two-day National Dialogue on "Water Conflicts in India—the State, the People and the Future" organised by NIAS (IWP Zonal Partner), Bangalore, March 15–16, 2010.
- T.S. Papola participated and chaired a session in UNESCO-ICSSR Research Meeting on *Social Protection Policies in South Asia*, ICSSR, New Delhi, March 18, 2010.
- Mahua Paul presented two papers on "Forecasting Turning Points of Economic Time Series: A study for India" and "Exchange Rate Pass Through and the J-curve: An Examination with the Indian Data" at the International Conference on *Quantitative Methods in Money, Banking, Finance and Insurance*, jointly organised by IBS Hyderabad and IGIDR Mumbai, March 19–20, 2010.
- S.R. Hashim participated in Annual Conference of Indian Association of Social Science Institutions (IASSI) entitled, *Conference and Ph.D. Workshop on Frontier Issues in Technology, Development and Environment* organised by Madras School of Economics at Chennai, March 19–21, 2010.
- T.S. Papola participated and chaired a session in Panel Discussion on *Human Development and Social Protection in the 21st Century: Evidence-Based Policy Design* organised by National Council of Applied Economic Research (NCAER), New Delhi, March 26, 2010.
- Jesim Pais and Partha Pratim Sahu made a presentation on "Structural Changes in Indian Economy: A Study of Subcontracting in the Unorganized Manufacturing Sector", March 29, 2010. This is part of the ICSSR sponsored research programme on "Structural Changes, Industry and Employment in the Indian Economy: Macro Economic Implications of the Emerging Trends".
- Nasir Tyabji made a presentation on "The Private Industry and the Second Five Year Plan: The Mundra Episode and Capitalist Cupidity", March 30, 2010.
- Satyaki Roy delivered two lectures on "Emerging Trends in Employment in India" and "Some Reflections on the Debate on Missing Middle" to IES Probationers undergoing training at the Institute of Economic Growth, March 30, 2010.
- P.L. Beena presented a paper on "Economic Liberalisation and Financing Pattern of Indian Industries" at the 4th Annual Conference on *The Global Economic Crisis and the Restructuring of the Financial and Trading System: Implications and Prospects for the Developing World* organised by the Witwaterstrand University, Johannesburg, April 08–10, 2010.
- Surajit Mazumdar gave a presentation on "Structural Changes in India's Agricultural Sector Since Independence", April 09, 2010. This is part of the ICSSR sponsored research programme on "Structural Changes, Industry and Employment in the Indian Economy: Macro Economic Implications of the Emerging Trends".
- T.S. Papola participated and chaired a session in *International Consultation on Rural Transformation* organised by Planning Commission and Institute for Human Development, New Delhi, April 14–16, 2010.
- Sunanda Sen gave a lecture on "China in the Global Economy", at ATWS, Jamia Millia Islamia, April 20, 2010.

- T.S. Papola presented a paper on "Structure of India's Economic Growth" in the Conference on *Growth and Development: Future Directions in India*, Centre for International Trade and Development, School of International Studies, Jawahar Lal Nehru University, April 23, 2010.
- Nasir Tyabji chaired the session on "Technology" at the Conference on *Growth and Development: Future Directions for India* organised by the Centre for International Trade and Development, School of International Studies, JNU, April 24, 2010.
- Satyaki Roy presented paper on "Garments Industry in India: Some Reflections on Size Distribution of Firms" in the International Workshop on *Trends in Manufacturing Employment in India and Bangladesh,* April 28–29, 2010 at Bangladesh Institute of Development Studies (BIDS), Dhaka.

## Visit of Foreign Scholars

- Three research scholars, Dr Wang Xiaomin, Mr Ye Hailin, & Dr Wu Zhaoli, from Chinese Academy of Social Sciences (CASS) visited ISID on January 14, 2010 under ICSSR-CASS bilateral programme. The purpose of the meeting was to exchange views with ISID Faculty members on issues relating to (i) the impact of financial crisis in India; (ii) India's regional policy and Chinese role in the regional issues of the sub-continent; and (iii) India's economic reforms, achievements and problems.

*Scholars from Chinese Academy of Social Sciences (CASS) interact with ISID faculty*

## Post-Doctoral Research Programme

- Dr Amba Pandey, who was awarded two years ICSSR Post-Doctoral General Fellowship to work on "India and its Diaspora in South-East Asia: Policy Initiatives" completed the study and joined her parent organisation Jawahar Lal Nehru University on February 05, 2010.
- Dr Abha Mathur, who was awarded two years ICSSR Post-Doctoral General Fellowship to work on "Environmental Impact of Industrialization: Study of Two Industrial Areas of Alwar District of Rajasthan" completed the study and joined her parent organisation L.B.S. Government College, Kotputli, Rajasthan on March 25, 2010.

# FACILITATING RESEARCH

## New Databases

The ISID has been acquiring new databases and updating the existing databases to meet the data requirements of researchers in the area of developmental and industrial processes with special emphasis on corporate sector, foreign investment, technology, international trade, labour and employment. The following new databases have been added recently:

- Annual Survey of Industries (Tabulated Data)—All India and State level (2, 3 & 4 digit levels): 2002–03 to 2006–07
- Annual Reports Database of BSE and NSE listed Companies: 2008–09 & 2009–10
- CapEx Database of CMIE
- PE/VC Deal Database, M&A Deal Database and PE Real Estate Deal Database
- National Accounts Statistics (EPWRF)
- Domestic Product of States of India 1960–61 to 2006–07: 2nd Edition (EPWRF)

## Library Upgradation

During this period, the following readings have been added to ISID's library collection—

- *The Elgar Companion to Classical Economics*, Vols. 1 & 2, Edited by Heinz D. Kurz and Neri Salvadori, Edward Elgar, 1998;
- *Capital Theory*, Vols. 1, 2 & 3, Edited by Christophere Bliss, Avi J. Cohen and G C Harcourt, Edward Elgar, 2005;
- *Amartya Sen: Critical Assessments of Contemporary Economists*,Vols. 1–5, Edited by John Cunningham Wood and Robert D. Wood, Routledge, 2007;
- *Input Output Analysis*, Vols. 1, 2 & 3, Edited by Heinz D. Kurz, Erik Dietzenbacher and Christian Lager, Edward Elgar, 1998;
- *Handbook of Regional Growth and Development Theories,* Edited by Roberta Capello and Peter Nijkamp, Edward Elgar, 2009;
- *International Handbook of Development Economics*, Vols. 1 & 2, Edited by Amitava K. Dutt and Jaime Ros, Edward Elgar, 2008.

## Staff News

Some of the supporting staff members who have been working with ISID for a long period on consolidated basis were regularised on May 1, 2010. The staff members who were regularised include:

- Shri Dinesh Kumar *Maintenance Assistant (Guest-House)*;
- Shri Shambhu Kamti *Maintenance Assistant*;

*Appointment letters are being handed-over to newly regularised staff members*

- Shri Brijesh Kumar *Maintenance Assistant (Plumber)*;
- Shri Acheylal *Maintenance Assistant (Electrician)*;
- Shri Sumit Sharma *Maintenance Assistant (Carpenter)*;
- Shri Jagbir Singh *Maintenance Assistant (Cook);* and
- Shri Madan Lal *Maintenance Assistant (Mason)*.

Shri Bhupesh Garg, who was working as *Programmer* has been promoted to *System Analyst*.

## OBSERVATIONS

### Current Account Balances, Investment and Growth in Developing Countries: The Odd Case of India

*Surajit Mazumdar*

The observation is based on work in progress that is rooted in a general perspective that the framework we adopt for analysing the trends and tendencies of the Indian economy needs to take into account what is happening in the global economy more explicitly than has been generally the case. It brings together three themes that have been the subjects of recent discussions but, separately from each other. The first of these is the peculiar feature of the world economy since the late 1990s that has been called the 'capital flows paradox' or the phenomenon of 'capital flowing uphill'. The second of these is the transition experienced by the Indian economy in the early years of the current century when the growth rates of her aggregate GDP, till the global crisis caused an interruption, moved to levels unprecedented in her history. The likelihood of the Indian economy reverting to that growth trajectory in the post-global crisis context is the final issue that I will discuss in conjunction with the other two.

#### The Paradox of Capital Flows

There are two parts to the paradox of international capital flows that have captured attention. The first is that unlike what mainstream theory predicts and what was the expected outcome of globalization, the direction of capital flows in the world economy before the global crisis had been from capital-scarce developing countries to the capital-abundant developed countries. This has mainly taken the form of accumulation of foreign exchange reserves by developing countries. The process of capital flowing uphill, of developing countries as a group running current account surpluses against deficits of developed countries, emerged after the East Asian crisis. Its scale, however, increased significantly from the early years of this century, during the 'third wave' of capital flows to and from developing countries[1]. This is, of course, an aggregate picture for the two groups of countries, and individual countries within each of them have exhibited in this period both current account surpluses as well as deficits. Broadly, however, the picture was one of improving current account balances amongst developing countries and the opposite in the case of developed ones. The second element in the paradox is that the capital flows have not been following growth, and instead the net capital exporting countries have been growing faster than the recipients of such flows. Developing countries as a whole experience a sharp upturn in their growth rates coinciding with the third wave of capital flows and created a large gap with the rates of developed countries. Even within them, the capital exporters were generally those with relatively higher investment and growth rates, typified by countries like China.

To explain the paradoxical combination of high growth and current account surpluses being exhibited by many developing countries, the UNCTAD's Trade and Development Report 2008 put forward, based on the work of Keynes and Schumpeter, an alternative to the mainstream analysis. In this view developing countries with diversified exports, like many East Asian countries, have been using competitive real exchange rates to generate export surpluses and accumulate foreign exchange reserves to reduce their vulnerability to volatile capital flows. This in turn allowed them to pursue monetary and fiscal policies encouraging investment financed by reinvested corporate profits and the banking system. Export surpluses and such domestic investment friendly policies worked towards stimulating demand and growth in these economies. Primary commodity exporting developing countries and oil-exporting countries on the other hand benefited from world demand conditions and rising prices after 2003. The Indian case, however, does not quite fit in with either of these stories.

#### The Case of India's High Growth

India's growth shifting into a higher gear from 2003–04 onwards was in line with the trend for developing countries as a whole, and ended the period of relative slow-down in growth into which the economy had slipped into in the second half of the 1990s. This was accompanied by a quite dramatic rise in the investment rate. For more than a decade prior to this, the ratio of Gross Capital Formation to GDP in India had stayed at the 25–26 per cent level, but in the short space of five years beginning 2003–04 it increased to nearly 39 per cent. In other words, a stimulation of investment was also part of the Indian story of acceleration in growth. Like many other developing countries, India, too, in this period accumulated large foreign exchange reserves. Where it was the most notable exception to the standard developing

[1] UNCTAD (2008)

country story was that while it was amongst the developing countries with the highest growths, it was a net capital importer rather than exporter during this phase. Its foreign exchange reserves were therefore accumulated on the basis of capital inflows rather than current account surpluses. One aspect of this was that capital inflows had also led to a sharp appreciation of the rupee which hurt Indian exports. Not only this, India's current account balance, and its merchandise balance, actually worsened in the period of high growth and rising investment rate. The merchandise balance in fact deteriorated to a much greater extent, attaining unprecedented levels (as a proportion of GDP). That not all of this was on account of oil imports is clear from the sharp deterioration that took place even in the non-oil balance. The non-oil balance and the current balance had both turned positive when growth was low, but this changed quite sharply once growth rates moved upward. India can thus be said to be an odd case amongst developing countries.

*Prof. Surajit Mazumdar delivering the ISID Foundation Day Lecture*

The correlation between rising investment rate and worsening current account balance in India's case did not, however, mean that rising investment was mainly financed by capital imports. In fact, compared to the rise in the investment rate the deterioration in current account balance was extremely limited. India's savings rate also increased concurrently, and to an order only marginally less than that of the investment rate. The notable aspect of this rise as well as of investment was that both were to a great extent attributable to the private corporate sector. The rather dramatic rise in the levels of private corporate investment since 2003–04 in turn is accounted for by the investment in manufacturing activities, the movement in the ratios of corporate and manufacturing investment to GDP being virtual mirror images of one another. This rapid growth of corporate and manufacturing investment reflected a spectacular recovery from the collapse that had characterized these in the six years prior to 2003–04 after the boom of the early 1990s.

The scorching pace of private corporate investment growth is clearly an important component of the story of high growth in India, and it indeed has been termed as an investment-led growth. On the demand side, this investment growth has clearly played a more important role than consumption growth, in whose case the pace of growth moved up relatively marginally. In fact the movement in growth rates, the slow-down in second half of the 1990s and the upward movement from 2003–04, shows a much stronger correlation with investment rather than consumption growth. In the recent phase of high growth, investment has more or less matched consumption in contributing to incremental demand.

In comparison to that in expanding demand, the supply side effect of rapidly growing corporate investment appears to have been more limited in the high-growth phase. While a large part of the investment went into manufacturing, the services contribution to output expansion was many times greater. An upswing in industrial growth, a recovery from the slump before that, did certainly happen but the pace of services growth stayed ahead of it. Services, of course, also accounts for a much larger share of India's GDP than industry, and even more in comparison to manufacturing. While industrial growth trends did reflect those exhibited by the manufacturing sector, within industry the most dramatic acceleration in growth occurred in construction.

### Explaining the Paradox within the Paradox

How then does one explain the transition of India to its high-growth phase if the crucial elements in the so-called typical story, export surpluses and improving current account balances, are missing in its case? I would like to put forward the hypothesis that the Indian case can be considered a special variant within that typical story.

Even if India's merchandise trade deficit worsened during the period of high growth, Indian exports of both goods and services did increase substantially faster during this phase. Moreover, the surge in exports began before growth picked up. As far as merchandise exports are concerned, export growth was accompanied by significant changes in both the direction of Indian exports as well as in its product composition. The share of developing countries and OPEC countries in Indian exports increased quite sharply indicating that the general growth story of these groups of countries was expanding demand for Indian exports. The products for which this demand was increasing most rapidly were not the items which traditionally dominated Indian exports, like textiles and gems and jewellery, but newer products. These new products—engineering goods (like iron and steel, metal manufactures, and transport equipment), chemical products, and petroleum products—assuming greater importance in Indian exports were different from India's traditional exports on one important count. Their requirement of capital per unit of output was much greater than the labour-intensive traditional exports. This and the export surge may have worked in conjunction to trigger the revival of corporate and manufacturing investment growth.

If the export surge did not contribute to an improving non-oil trade balance, it was because once investment and growth picked up, imports eventually outpaced exports even in the very same categories of products whose share in Indian exports was rising. The export surge and the changes in the composition of Indian manufactured exports cannot therefore be considered as indications of any significant export breakthrough. If the trend in merchandise trade had been all that was there, the growth would have been hard to sustain even for the period that it did. This is where the parallel growth of India's services exports as well as the large inflow of remittances, both dependent on external economic conditions, played a crucial role. Even as the merchandise balance was increasing very sharply, these kept India's current account deficit in check and within reasonable limits. This in turn maintained conditions necessary for the large capital inflows into India that occurred during this period, which financed not only the deficit, but enabled India to accumulate large foreign exchange reserves.

The surge of portfolio capital inflows began from 2003–04 onwards, and it has been pointed out that even a large part of FDI flows which picked up subsequently were of a similar nature[2]. This resulted in a prolonged stock-market boom which gave an impetus to spending in the economy. The rapid growth of corporate investment was also assisted by the boom in the capital issues and private placement markets this engendered, and also by external commercial borrowings. Additionally, speculative sentiments spilled over into the real estate sector and contributed to a construction boom. Apart from its direct effect on investment, this also expanded the demand for a range of manufacturing industries. High growth of corporate profits through its effect on corporate tax revenues enabled simultaneously both a faster growth of public expenditure than had been the case earlier as well as a shrinking of the fiscal deficit to GDP ratio. This reinforced the process of demand growth without making financial markets too nervous. All of these went into producing the mood of optimism that was prevalent in corporate India till the global crisis erupted.

### Is a Return to the Pre-Crisis Trajectory Possible?

If the analysis presented above is correct, then clearly India's high growth was not a purely Indian story. A 'favourable' international configuration did contribute to triggering and sustaining the investment boom which drove the growth process. More importantly, those favourable external conditions temporarily allowed the Indian economy to overcome certain structural weaknesses in whose presence even the maintenance of those conditions was unlikely to have been sufficient for sustaining the positive investment climate. These weaknesses, expressed in the form of the pace of investment in the manufacturing sector tending to outstrip manufacturing demand growth, had been responsible for the previous collapse in corporate investment in the 1990s. As indicated earlier, this imbalance was showing up again in the boom after 2003–04, and the rise in the manufacturing investment to GDP ratio was not matched by a corresponding increase in the importance of the manufacturing sector's share in total output. Another collapse of manufacturing and corporate investment was therefore imminent even without the global situation turning adverse. Indeed, it has been pointed out that the slow-down of growth and investment in India began even before the global crisis erupted in full force. With that eruption, the process was only cemented.

Clearly therefore a quick return to the specific growth trajectory that India traversed in the half-decade preceding the global crisis would appear to be very difficult. If it is to achieve similar levels of growth, the basis would need to be different given that neither global nor domestic economic conditions are the same as earlier. In this regard, I would like to draw attention to some features of India's growth in the last two years that appear in sharp relief when compared with the high growth phase. Most people note that the slow-down in growth in these two years has not been that dramatic and India has relatively speaking performed extremely creditably. What has been less highlighted is the fact that the slowdown in the pace of growth of the two most important components of demand, private consumption and investment, has been far sharper and their combined growth rate has been dragged down below that of GDP. In the last two years, some combination of fall in net indirect taxes, government consumption expenditure (pay commission effect), and decline in net imports, have propped up growth even when the main components of demand have lagged. Such propping up, however, can only be a temporary phenomenon. In the long run the growth rate will have to adjust to the pace of growth of investment and consumption. Both of these will need to increase dramatically if the pre-crisis growth trajectory is to be replicated. It is not, however, clear how these can happen. Another way of looking at, which adds to the scepticism about this, is the following. If India is to revert to a trajectory where real investment is growing at over 15 per cent per annum and GDP at 9 per cent or thereabouts, in five to six years the investment ratio would touch 50 per cent and cross 60 per cent in a decade or so. Is this a realistic scenario? I leave this for all of you to judge for yourselves.

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[2] K.S. Chalapati Rao, presentation at the symposium on *Concepts, Definition and Data Issues to FDI in India*, ISID, New Delhi, March 16, 2010.

## About the ISID

The Institute for Studies in Industrial Development (ISID), successor to the Corporate Studies Group (CSG), is a national-level policy research organisation in the public domain and is affiliated to the Indian Council of Social Science Research (ICSSR). Developing on the initial strength of studying India's industrial regulations, ISID has gained varied expertise in the analysis of the issues thrown up by the changing policy environment. The Institute's research and academic activities are organised under the following broad thematic areas:

*Industrial Development:* Complementarity and performance of different sectors (public, private, FDI, cooperative, SMEs, etc.); trends, structures and performance of Indian industries in the context of globalisation; locational aspects of industry in the context of balanced regional development.

*Corporate Sector:* Ownership structures; finance; mergers and acquisitions; efficacy of regulatory systems and other means of policy intervention; trends and changes in the Indian corporate sector in the background of global developments in corporate governance, integration and competitiveness.

*Trade, Investment and Technology:* Trade policy reforms, WTO, composition and direction of trade, import intensity of exports, regional and bilateral trade, foreign investment, technology imports, R&D and patents.

*Employment, Labour and Social Sector:* Growth and structure of employment; impact of economic reforms and globalisation; trade and employment, labour regulation, social protection, health, education, etc.

*Media Studies:* Use of modern multimedia techniques for effective, wider and focused dissemination of social science research and promote public debates.

ISID has developed databases on various aspects of the Indian economy, particularly concerning industry and the corporate sector. It has created Online Indexes of 150 Indian Social Science Journals (OLI) and 15 daily English Newspapers. More than one million scanned images of Press Clippings since 1999 on diverse social science subjects are available online to scholars and researchers. These databases have been widely acclaimed as valuable sources of information for researchers studying India's socio-economic development.


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