Chapter 4

Government Policies for Business Growth

By C.A , I.S.A , M.A (Eco) , B.com
Mrugesh Madlani

Comparision between Policy Regime of mid fifties with Policy after 1990's

POLICY REGIME OF MID FIFTIES	POLICY REGIME SINCE 1990'S
Nature of Economic System Mixed Economy with dominant public sector	Capitalistic Economy
Instrument of Economic Governance Economic Planning	Market Mechanism
Openness Orientation Closed economy policies	Open economy policies
Role of Government in Business Acquiring Heights through PSU's	State ownership as exception , Privatisation of PSU's
Role of Government Regulation & Control	Liberalisation of regulations

Economic Government Policies for Business

- **Macroeconomic Management – Affect all sectors of economy**

1. Fiscal Policy – Government revenue and expenditure
2. Monetary Policy- Supply of money , credit

- **Sector Management – Applicable for particular sector**

1. Agricultural Policy
2. Industrial Policy
3. Foreign Trade & Investment Policy

- All Aspects of Business are influenced by government policies.
- These policies affect start ups and business registration , dealing with consumers , and even exit
- There are central and state government policies also
- These economic policies affect both demand or supply side or both

Macro Policy Indicators & Business Conduciveness

- **GDP , Inflation , Tax rates , Interest rates & Exchange rates** are most significant macro policy indicator that impact business
- Growing GDP is indicator of high demand , thus it leads to repetitive cycle whereby high demand means growth opportunity , greater investment which leads to greater production , which leads to greater income generation , thereby creating greating demand and hence lasting growth
- Moderate Inflation also bring positivity for Business as rising prices leads to opportunity trigger for higher profitability

- Lower Interest rates would make investment in projects easier and hence companies can expand their business portfolios and also will reduce their cost of capital , increasing ROI
- Lower Tax Rates increase Business Investments and higher Tax rates will reduce investments
- Moderate exchange rate that is high external value of domestic currency helps Business in 2 ways

1. One by making imports expensive , so we will look for substitutes
2. Secondly by increasing exports as they are cheaper as per International markets and increasing Exports and reducing imports helps to increase GDP

Policy Formulation & Impact Transmission Process

- Policy are framed as per aspirations of the nation
- Ultimate responsibility of policy formulation lies with concerned ministry
- Ministry in turn functions through committees , commissions and institutions
- Draft Policies are put in public domain for comments , critique and suggestions
- Policies are then implemented and impact is felt
- There can be several ways of implementing policies

Types of Government Policy by Intended Impact

- **Protective Policies –** Aim to provide protection to businesses so they can sustain themselves and grow . Eg – In 1970's few business were reserved for small sector , Mid fifties to eighties restricting entry of multinational corporations in India
- **Restrictive Policies** curtail all the benefits in some particular issue . Eg – higher rate of custom duty on imports
- **Regulatory Practices** regulate the activities of particular sector of the economy. Eg – RBI – Banks , SEBI – Capital Markets , Corporate Function – Companies Act
- **Facilitating Policies** are ones which facilitate an activity . Eg – MSME ,Make In India for industrial activity , Start up India

Liberalization

- It means to remove or loosen restrictions. It happens via dismantling of licenses , permits , ease of approvals and systematic loosening of legislative and administrative controls over business.
- There were lot of restrictions like number of industries for public sector , obtaining licenses for capacity installation and increase , reservation of items for small scale industries
- Liberalization is systematic process of enlargement and enhancement of freedom of private sector in economy .

Winds of Change – Industrial Liberalization

- List of Industries for Public Sector which was 18 like Telecomm , iron & steel , Mineral oil , electricity generation and distribution ,reduced to 3 – Defence aircrafts and warships , atomic energy generation and Railway Transport
- Industrial Licensing by Central Govt abolished except for hazardous and sensitive industries like alcohol , ciggarates , industrial explosives , aerospace , Drugs and Pharmaceuticals
- Large Industrial Houses needed separate clearance under MRTP Act removed and better Competition Law came
- About 800 Items were produced only by small scale sector like Toys , Garments , Shoes was removed , to increase India's export & growth

Privatization

- It is managerial approach of changing the ownership structure of one or more government institutions

- In India it was hard because all were loss making units. Government decided to privatize loss making companies fully , profit making ones and banks partially

Privatization can be done in following ways

- **Delegation** – Ownership will be of government , but they will be management by private sector. It can be through contract , franchise , grant
- **Divestment** – Government surrenders partial ownership and responsibility and sells majority stake to one or more private entities. Eg - (Hindustan Zinc – Vedanta Resources)
- **Disinvestment** – Selling portion of ownership in public enterprise to private party , but ownership is still with Government . Eg – AirIndia Government planning to do Disinvestment
- **Displacement** – Private sector expands and displaces government entity . Eg – Telecomm companies due to privatization have displaced BSNL & MTNL

Foreign Direct Investment

- FDI is flow of capital investment in enterprise in a nation by another enterprise in different nation by capturing majority stake in ownership of that country or expanding operations of existing business in that country
- Some sectors FDI allowed is 100 % and some upto 26 , 49 or 51 %
- In certain areas FDI limit has been capped like Insurance , in case there is no approval through automatic route , we need to seek permission from Foreign Investment Promotion Board

FDI Sectors wise

- 26 % - FM Radio , Print media , Public sector banks max – 20 %
- 49% - Petro-refinery(Indian oil) , Defense , Cable , Insurance , Airlines , Private security agencies
- 51 % - Multi-brand retail (Showroom of multiple brands)
- 100% - Single brand retail (Showroom of single brand)

Few Sectors where FDI as been prohibited by automatic as well as government route

- Atomic Energy
- Lottery Business
- Gambling & Betting
- Business of chit Fund
- Nidhi Company
- Agriculture (Except Horticulture , Floriculture , Pisciculture , Animal Husbandry , Development of seeds & mushrooms under controlled condition)
- Tree Plantation (Except Tea Plantation)
- Housing & real estate (Except Township , Residential / Commercial premises , roads or bridges etc)
- Trading in Transferable Development Rights
- Manufacture of cigars , cheroots , cigarillos , of tobacco or tobacco substitutes

Foreign Institutional Investors (FII)

- FII are large groups with substantial investible funds . They are registered abroad and invest in other nations markets , hedge funds , pension funds . They have strong research team
- They parks funds to bullish market and when market is at peak , and starts declining , they move funds to another nation , and market falls down of that nation
- So government believes more in FDI rather than FII . Eg – Europacific Growth Fund , Government of Singapore , Oppenheimer

OFDI (Outward Foreign Direct Investment)

- Policy of Globalization favoured India not only in terms of inward FDI , but also Outward FDI
- Indian firms invest abroad too