STUDY MATERIAL

PROFESSIONAL PROGRAMME

INTERNATIONAL BUSINESS – LAWS AND PRACTICES

MODULE 3

ELECTIVE PAPER 9.5

THE INSTITUTE OF
Company Secretaries of India
IN PURSUIT OF PROFESSIONAL EXCELLENCE
Statutory body under an Act of Parliament

ICSI House, 22, Institutional Area, Lodi Road, New Delhi 110 003
tel 011-4534 1000, 4150 4444 **fax** +91-11-2462 6727
email info@icsi.edu **website** www.icsi.edu

© THE INSTITUTE OF COMPANY SECRETARIES OF INDIA

TIMING OF HEADQUARTERS

Monday to Friday

Office Timings – 9.00 A.M. to 5.30 P.M.

Public Dealing Timings

Without financial transactions – 9.30 A.M. to 5.00 P.M.

With financial transactions – 9.30 A.M. to 4.00 P.M.

Phones

41504444, 45341000

Fax

011-24626727

Website

www.icsi.edu

E-mail

info@icsi.edu

Laser Typesetting by AArushi Graphics, Prashant Vihar, New Delhi, and
Printed at Tan Prints/..... 2015

INTERNATIONAL BUSINESS - LAWS AND PRACTICES

Today globalization has dramatically re-shaped the markets and has changed the way business is being done. One has to keep pace with the customer's requirement and has to bring in services and products as per global standards. International trade has become a vital component of development strategy, which can be used as an effective instrument of economic growth. Moreover the establishment of institutions like World Trade Organisation has ushered a new era of global economic co-operation reflecting the widespread desire to operate in a more open multilateral trading system. Participation in international trade has become necessity for all countries and as well as companies for growth.

Thus it becomes important for professionals to acquire knowledge and skill to help work in international companies and in global environment. Having updated knowledge of international business laws and procedures becomes key requisite for professionals. So, in this study broad aspects related to international business environment, export management, FDI policy, FTP policy, international trade theories, international trade bodies like WTO, UNCTAD, international logistics and supply chain etc. has been discussed in detail. Added emphasis has been laid on strategic alliances, foreign collaborations and joint ventures abroad, to enable the students to discharge efficient services and to tackle practical situations.

In this study every efforts has been made to give a comprehensive coverage of all the topics relevant to the subject. At the end of each study lesson a brief about the lesson have been given under the caption '**Lesson Round Up**' as well as questions have been given under the caption '**Self Test Questions**' for the practice of students to test their knowledge.

This study material has been published to aid the students in preparing for the **INTERNATIONAL BUSINESS – LAWS AND PRACTICES** paper of the CS Professional Programme. It is part of the education kit and takes the students step by step through each phase of preparation stressing key concepts, pointers and procedures. Company Secretaryship being a professional course, the examination standards are set very high, with emphasis on knowledge of concepts, applications, procedures and case laws, for which sole reliance on the contents of this study material may not be enough.

Therefore, in order to supplement the information/contents given in the study material, students are advised to refer to the Suggested Readings mentioned in the study material, Student Company Secretary, Business Dailies and Journals.

In the event of any doubt, students may write to the Directorate of Academics in the Institute for clarification at **academics@icsi.edu.**

Although due care has been taken in publishing this study material yet the possibility of errors, omissions and/or discrepancies cannot be ruled out. This publication is released with an understanding that the Institute shall not be responsible for any errors, omissions and/or discrepancies or any action taken in that behalf.

Should there be any discrepancy, error or omission noted in the study material, the Institute shall be obliged if the same are brought to its notice for issue of the corrigendum in the e-bulletin Student Company Secretary.

There is open book examination for this Elective Subject of Professional Programme. This is to inculcate and develop skills of creative thinking, problem solving and decision making amongst students of its professional programme and to assess their analytical ability, real understanding of facts and concepts and mastery to apply, rather than to simply recall, replicate and reproduce concepts and principles in the examination.

SYLLABUS

ELECTIVE PAPER 9-5 : INTERNATIONAL BUSINESS - LAWS AND PRACTICES

Level of Knowledge: Expert Knowledge

Objective: *To acquire specialized knowledge in International business, law, procedure and practices.*

Detailed Contents:

1. **Introduction**
   - International Business - Nature and Scope,
   - Globalization - Meaning, Levels, Merits, Limitations and irreversibility of Globalization
   - Need to go global
   - Internationalization Decisions (entry modes)
2. **International Business Environment**
   - Meaning of Environment
   - Dimensions - PEST to STEEPLE
   - SWOT Analysis
   - Various approaches to Assess competitiveness including Michael Porter's 5- Forces Model
   - Global Competitiveness Index
3. **Multi National Enterprises (MNEs) and Foreign Direct Investment (FDI)**
   - Meaning and Characteristics
   - Role of MNEs in host economy
   - FDI Policy of India
   - Trends in Global FDI
   - Trends in FDI with reference to India
   - Issues with MNEs - Taxation, Restrictive Trade Practices, Currency, Jurisdiction and Technology Transfer
4. **Foreign Trade Policy and Procedures**
   - Introduction to Foreign Trade Policy
   - Institutional Framework for Export Promotion
   - Export Incentives and Facilities
   - EPZ/FTZ/100% EOUs
   - Quality Control for Exports
   - Export Prospects for Select Products and Services
   - INCO Terms

- International Commercial Arbitration-Pre Shipment and Post Shipment Finance
- SEZ-Incentives and Benefits
- Method of Realizing Export Payments and Ensuring Guaranteed Export Payment
- Central Excise Clearance Formalities
- Customs Regulations and Clearance Formalities for Exports & Imports
- Duty Draw Back Claims Procedure
- Foreign Trade Financing - Export & Import
- Foreign Exchange Risk Management
- International Credit Management
- Warehousing
- Instruments of Trade Policy and India's Trade Policy

5. International Trade and Regional Economic Integration

- Theory - Mercantilism, absolute advantage and comparative advantage
- Trends in Global Trade
- Trends in India's Trade
- Types of Regional Economic Integration - Free Trade Area, Custom Union, Common Market, Economic Union, Monitory Union and Political Union etc.
- Trading Blocks- ASEAN,SAFTA,SAARC,NAFTA,EU

6. Institutional Environment

- Pre WTO Scenario, difference between GATT and WTO
- Trade Related Institutions - WTO and UNCTAD
- WTO - Basic Principles, various agreements, Functions and Areas of Operations, Dispute Settlement Mechanism (rules and procedures)
- IMF, IBRD, ADB
- Commodity Agreements

7. Anti-Dumping Duties

- WTO Provisions on Anti-Dumping-, Anti-Dumping Duties, Procedure and Developments
- Regulatory Framework for Anti Dumping in India
- Recent Anti Dumping Cases in India

8. Subsidies and Countervailing Duties

- WTO Provisions
- Administration
- Procedure and Emerging Trends
- Regulatory Framework for Subsidies & Countervailing duties in India
- Doha Development Round

9. **Foreign Collaborations and Joint Ventures**
   - Kinds of Collaboration and Joint Ventures
   - Drafting of Agreement
   - International Commercial Arbitration
10. **Strategic Alliances**
   - Meaning, Rationale, Types, Trends in Alliances in New Competitive Environment, Strategic Alliance Failures, Managing Strategic Alliances.
11. **Logistics Management**
   - Logistics Framework- Concept, Objective and Scope
   - Transportation, Warehousing, Inventory Management, Packing and Unitization, Control and Communication
   - Role of IT in Logistics, Logistics Service Firms and Third Party Logistics

LIST OF RECOMMENDED BOOKS

MODULE 3

ELECTIVE PAPER 9-5 : INTERNATIONAL BUSINESS - LAWS AND PRACTICES

The students may refer to the given books and websites for further knowledge and study of the subject :

Books :

- International Trade and Export Management by Francis Cherunilam , Himalaya publishing House
- International Business by K Awasthappa, Mc Graw Hill
- Foreign Trade Policy and Handbook of Procedures by R.K.Jain (17th Edition 2012)
- Anti Dumping Law and Procedures by R.K.Gupta (4th Edition 2013)
- International Business – Justin Paul, PHI Publications
- A Guide to Export-Import Consultancy & Registration Services V.K.Pamecha, Paper Bac
- Export Management, P.K.Khurana, Paper Back
- Guide to the WTO & GATS – A.K. Koul, Satyam Law

Websites :

- www.wto.org
- www.imf.org
- www.adb.org
- www.unctad.org
- www.worldbank.org
- www.finmin.nic.in
- www.commerce.nic.in
- www.saarc-sec.org
- www.iccwbo.org
- www.rbi.org.in
- www.asean.org
- www.europa.eu
- www.sapta.co.in
- www.naftanow.org

CONTENTS

INTERNATIONAL BUSINESS - LAWS AND PRACTICES

LESSON 1

INTRODUCTION TO INTERNATIONAL BUSINESS

Business	2
International Business	2
Drivers of International Business	2
Benefits of International Business	4
Scope of International Business	5
Difference between domestic and international business	5
Globalisation	8
Meaning of Globalisation	8
Benefits of Globalisation	10
Criticisms of Globalisation	11
MYTHS about Globalization	11
Stages of Globalisation	12
Risks in Global Business	13
Issues in Global Business	14
Globalisation and International Trade	15
Globalisation and Financial Markets	15
Globalization, Income Inequality and Poverty	16
Globalisation and Strategic Management	17
The Future of Globalization	18
Globalisation of India	18
Needs to Go Global	20
Modes of Entry and Operation in International Business	23
Walmart's Entry through the World – Case study	23
Exporting	25
Licensing	25
Franchising	26
Special Modes	28
Contract Manufacturing	28

Page

Management Contracts 29
Turnkey Projects 29
Foreign Direct Investment without Alliances 29
Foreign Direct Investment with Strategic Alliances 30
Mergers and Acquisitions 30
Joint venture 30
Case Study - Entry strategies of Starbucks 30
LESSON ROUND UP 33
SELF TEST QUESTIONS 34

LESSON 2

INTERNATIONAL BUSINESS ENVIRONMENT

Business environment 36
International Business environment 36
Political Environment 37
Economic Environment 38
Technological Environment 38
Cultural Environment 39
Competitive Environment 40
Tools for International business environment analysis 40
Pest Analysis 40
PEST and SWOT 44
PEST variations 44
PESTEL model 45
Case study - Premier Inn's PESTLE Analysis 46
SWOT Analysis 49
Guidelines for successful SWOT 51
SWOT analysis template 52
Porter's Five Forces model 55
Performing the Analysis 57
Case study - Porter's Five Forces Analysis of Indian Automobile industry 58
Global Competitiveness index 61
The 12 Pillars of Competitiveness 61

Page

The interrelation of the 12 pillars 65

Stages of development and the weighted index 66

The Global Competitiveness Index (GCI) 2013-14 Rankings 67

The Global Competitiveness Index (GCI) of India 2013-14 67

LESSON ROUND UP 68

SELF TEST QUESTIONS 68

LESSON 3

Multinational Enterprises (MNEs) and Foreign Direct Investments (FDI)

Multinational Enterprises / Multinational Corporations 70

Characteristics of Multinational Corporations 71

Forms of Multinational Corporations 72

Role of Multinational Corporations 73

Benefits to Host Country 73

Benefits to Home Country 74

Criticism of Multinational Corporations 74

Issues with Multinational Corporations 75

Foreign Direct investment (FDI) 76

Meaning and Definition 76

Importance of FDI 77

Advantages of FDI 78

Disadvantages of FDI 78

Industrial policy of india 78

Industrial Policy Resolution, 1948 79

Industrial Policy Resolution, 1956 80

New Industrial Policy, 1991 80

FDI Policy Framework in India 81

Role of Department of Industrial Policy & Promotion 82

FDI Policy of India 82

Foreign Investment Implementation Authority (FIIA) 96

Case Study on FDI Policy: The International Experience 97

Case Study : Cross-Country Comparison of FDI Policies – Where does India stand? 101

LESSON ROUND UP 103

SELF TEST QUESTIONS 104

Page

LESSON 4

FOREIGN TRADE POLICY AND PROCEDURES – PART I - EXPORT MANAGEMENT

Foreign Trade	106
Foreign Trade Policy 2015-2020	106
Highlights of the FTP 2015-2020	107
Special Economic Zone	111
Free Trade and Warehousing Zones	114
Institutional Framework for Promotion of Exports	116
Ministry of Commerce	117
Autonomous Bodies/ Public Sector Undertakings/ Export Promotion Councils/ Other Organizations under Ministry of Commerce	120
Public Sector Undertakings under Ministry of Commerce	123
Export promotion council	124
Registered Export Promotion Councils	125
EPCS under the Administrative Control of the Department of Commerce	125
Other Organisations under Ministry of Commerce	128
Federation of Indian Export Organisations	128
Indian Council of Arbitration, New Delhi	128
Indian Diamond Institute, Surat	128
Footwear Design & Development Institute (FDDI)	129
National Centre for Trade Information	129
Price Stabilization Fund Trust	129
GS1-India	129
Advisory Bodies	130
Board of Trade (BOT)	130
Terms of reference of the Board of Trade	130
Inter State Trade Council	130
Attached and Subordinate Offices	130
Directorate General of Foreign Trade (DGFT)	130
Directorate General of Supplies and Disposal (DGS&D)	131
Directorate General of Anti-Dumping & Allied Duties (DGAD)	131
Directorate General of Commercial Intelligence and Statistics (DGCI&S)	131
Offices of Development Commissioner of Special Economic Zones (SEZs)	132

Page

Pay and Accounts Office (Supply) 132
Pay and Accounts Office (Commerce & Textiles) 132
Exim Bank of India 132
LESSON ROUND UP 134
SELF TEST QUESTIONS 135

LESSON 5

FOREIGN TRADE POLICY AND PROCEDURES - PART II – EXPORT MANAGEMENT

Concept of Export 138
Reasons for Export 138
Planning for Export 138
Product Selection 139
Market Selection 140
General Provisions Regarding Imports and Exports 141
Registration of Exporters 141
Registration with Reserve Bank of India (RBI) 141
Registration with Director General of Foreign Trade (DGFT) 141
Registration with Export Promotion Council 141
Registration with Commodity Boards 142
Registration with Income Tax Authorities 142
Importer Exporter Code Number (IEC) 142
Export License 146
Inquiry and Offer for Exports 147
Sample Exports 147
Export Pricing 148
Incoterms 149
Rules for any mode or modes of transport/Multi modal transport 150
Rules for Sea and Inland Waterway Transport 151
Rules for domestic and international trade 151
Export Documents 151
Pre-shipment Documents 152
Post Shipment Documents 152
Documents Related to Goods 153

	Page
Documents Related to Payment	154
Documents Related to Inspection	154
Documents Related to Excisable Goods	155
Certificates Related to Shipment	155
Terms of payment or methods of payment	156
Payment in Advance	157
Open Account	157
Documentary Collections	158
Documents against Payment (D/P)	159
Documents against Acceptance (D/A)	159
Letter of credit	160
Export Financing	166
Pre-shipment / Packing Credit	168
Stages of Granting Pre Shipment Credit to Exporter	169
Types of Pre-shipment Rupee Export credit	170
Pre-shipment Credit in Foreign Currency (PCFC)	172
‘Post-shipment Credit	173
Types of Post Shipment Rupee export credit	173
Post-shipment Credit In Foreign Currency	175
Factoring and forfaiting	175
Export Factoring	176
Forfaiting	177
Quality Control & Pre Shipment inspection	179
Packing and Labeling of Goods	181
Central Excise Clearance Procedure for Export	182
Procedure for export to all countries (except Nepal and Bhutan) under payment of duty	182
Procedure for Export to all Countries (Except Nepal and Bhutan) Without Payment of Duty	184
Customs Procedure for Export	186
Export Risk Management	189
Export credit insurance	191
Export credit guarantee	192
LESSON ROUND UP	193
SELF TEST QUESTIONS	195

Page

LESSON 6

INTERNATIONAL TRADE AND REGIONAL ECONOMIC INTEGRATION

International Trade – Meaning	198
Difference between international and domestic trade	198
Reasons for international Trade	198
Theories of International Trade	200
Mercantilism	200
Theory of absolute advantage by Adam Smith	201
Theory of comparative advantage by david ricardo	201
Hecksher ohlin Model	203
New Trade Theory: by Paul Krugman	203
Regional Economic Integration	216
Regional Trading blocs	217
Types of Regional trading blocs	217
Advantages of Regional trading blocs	218
Disadvantages of Regional trading blocs	218
Important Regional Trading Blocks	219
1. Association of South-east Asian Nations (ASEAN)	219
2. European Union	221
3. North American Free Trade Agreement (NAFTA)	224
4. South Asian Association for Regional Cooperation (SAARC)	226
5. South Asian Preferential Trading Area	228
6. South Asian Free Trade Area (SAFTA)	228
LESSON ROUND UP	231
SELF TEST QUESTIONS	231

LESSON 7

INSTITUTIONAL ENVIRONMENT

World Trade Organization	234
Overview	234
Principles of the Trading System	235
Trade without Discrimination	235
Freer Trade: Gradually through Negotiation	236

	Page
Predictability: Through Binding and Transparency	236
Promoting Fair Competition	237
Encouraging Development and Economic Reform	237
History and Formation of WTO	237
GATT: ‘Provisional’ for Almost Half a Century	237
The Tokyo Round: A First Try to Reform the System	238
Did GATT succeed?	239
The Uruguay Round	239
A round to end all rounds?	240
What happened to GATT?	241
The post-Uruguay Round built-in agenda	241
How is the WTO different from GATT?	242
Dispute Settlement Mechanism	242
Principles of Dispute Settlement	243
Comparison of Dispute Settlement Under GATT and Uruguay Round	243
How are disputes settled?	243
The Panel Process	244
Diagramatic Representation of the Panel Process	246
Case Study - Dispute Settlement System of the WTO	246
Introduction	246
WTO Structure	248
WTO Secretariat	249
The WTO Agreements	249
Agreement on Tariffs	250
The Agriculture Agreement	251
Agreement on Standards and safety	251
Agreement on Textiles	252
Agreement on Trade in Services	253
Agreement on Intellectual Property	254
Agreement on Safeguards	256
Agreements on Non-tariff Barriers: Red Tape, Etc	258
Agreement on plurilaterals	259
Agreement on Trade Policy Reviews	260

	Page
United Nations Conference on Trade and Development (UNCTAD)	262
Members	262
UNCTAD Conferences	264
History of UNCTAD	264
Main Goals	266
Main Activities	267
Relationship with Other Agencies	268
UNCTAD and Civil Society	268
UNCTAD´s Programme Budget and Financing of Technical Cooperation Activities	269
Evaluation at UNCTAD	269
International Commodity Agreements	270
World Bank	273
Members	273
Organisation	274
Functioning of the world bank	274
Contributions of the World bank	274
India and the World Bank	275
International Monetary Fund (IMF)	278
Goals of IMF	279
Surveillance	279
Financial assistance	280
SDRs	280
Technical assistance	280
Resources	280
Governance and organization	280
India and the IMF	281
Asian Development Bank	281
Key achievements	282
Members	282
Regional Members	283
Non-regional Members	283
Board of Governors	284
Board of Directors	284

	Page
Management	284
Policies and Strategies	284
History	284
Working of ADB	285
India and ADB	286
LESSON ROUND UP	288
SELF TEST QUESTIONS	289
LESSON 8	
ANTI DUMPING DUTIES	
Dumping	292
Anti Dumping	292
Difference between Anti Dumping duty and Normal Customs duty	292
WTO – Provisions on Anti Dumping	292
Article VI of GATT and the Anti-Dumping Agreement	293
Anti-Dumping Agreement	294
Basic principles of the Anti Dumping Agreement	294
Committee on Anti-Dumping Practices	294
Dispute Settlement	295
Notifications	295
Dumping	295
Determination of Normal Value	296
Determination of Export Price	297
Fair Comparison of Normal Value and Export Price	298
Calculation of Dumping Margins and Duty Assessment	298
Determination of Injury and Casual Link	299
Injury	300
Elements of Analysis	301
Investigation	302
Provisional Measures and Price Undertakings	303
Collection of Duties	303
Review and Public Notice	304
Regulatory Framework for Anti Dumping in India	304

Page

Institutional Arrangement in India for Anti Dumping 305

Anti Dumping Duties – Procedures in India 305

Anti Dumping Cases Initiated by India 312

Recent Anti Dumping Cases in India 313

Case Study - The Indian Shrimp Industry Organizes to Fight the Threat of Anti-Dumping Action 316

LESSON ROUND UP 322

SELF TEST QUESTIONS 323

LESSON 9

SUBSIDIES AND COUNTERVAILING DUTIES

Subsidy 326

Difference between dumping and subsidy 326

Countervailing duty 326

Anti dumping duty and countervailing duty 326

WTO Provisions on Subsidies and Countervailing Duties 327

Agreement on Subsidies and Countervailing Measures 328

Structure of the Agreement 328

Definition of subsidy 329

Definition of Specificity 330

Categories of subsidies 330

Countervailing Measures 332

Parameters Determining Countervailing Measures 333

Determination of Injury 333

Definition of Injury 333

Causal Link 334

Assessment of Subsidy 334

Guidelines for Determination of Subsidy 334

Transition Rules and Special and Differential Treatment 334

Notification 335

Countervailing Legislation and Measures 335

Dispute Settlement 335

Procedural Matters 335

Making an Application for Investigation into Countervailing Measures 335

Contents of the Application 336

Page

Processing of the Application by the Investigation Authority 336
Whether Application from Domestic Industry is Necessary to Initiate Investigation? 336
Whether Investigation is to be Initiated in all Cases? 336
Time-limit to Conduct the Investigation 336
Transparency in Investigation Process 336
Manner under which the Investigation is Conducted 337
Legal Framework with respect to Imposition of Anti-subsidy in India 337
Implementing Authorities in India 337
Doha Development Round 338
Case study - India's Export Subsidies on Textiles 340
LESSON ROUND UP 342
SELF TEST QUESTIONS 342

LESSON 10

FOREIGN COLLABORATIONS AND JOINT VENTURES

Foreign Collaboration 344
Examples of Foreign Collaboration 345
Features of Foreign Collaboration 346
Objectives of Foreign Collaboration 347
Types of Foreign Collaboration 347
Joint venture 348
Reasons for Forming a Joint Venture 350
Basic Elements of a Joint Venture 350
Structuring the Joint Venture 351
Managing the Joint Venture 352
Modes of Joint Venture 353
Equity Joint Venture 353
Contractual Joint Venture 353
Advantages of Joint Venture 355
Disadvantages of joint venture 356
Termination of Joint Ventures 356
Examples of Joint Ventures 357
Joint Venture Agreements 358
Drafting of a Joint Venture or Foreign Collaboration Agreement 362

Page

Specimen Joint Venture Agreement 363

International Commercial arbitration 367

Benefits of international commercial arbitration 369

UNCITRAL Model Law on International Commercial Arbitration 371

LESSON ROUND UP 382

SELF TEST QUESTIONS 383

LESSON 11

STRATEGIC ALLIANCES

Strategic Alliances: A Key Element of the Toshiba's Corporate Strategy 386

Introduction 386

Meaning and Definition 387

Advantages of Strategic Alliances 388

Disadvantages of strategic alliance 388

Types of Strategic Alliances 388

Strategic Alliance on the Basis of Type of Industry 389

Strategic Alliance on the Basis of Capital Commitments 389

Stages of Alliance Formation 389

Reasons for Creating Strategic Alliances 390

Managing Strategic Alliances 391

Strategic Alliance Failures 393

Trends in Strategic Alliances 395

Case Studies 396

Air India and Lufthansa Strategic Alliance 396

Joint Engineering Design by Ford and ABB 397

Strategic Alliance by AT&T 397

Strategic Alliance by NYPRO 397

LESSON ROUND UP 397

SELF TEST QUESTIONS 398

Lesson 12

Logistics Management

Logistics Management – Meaning and Definition 400

Objective of Logistics Management 401

	Page
Role of Logistics Management in an Organization	402
Stages in Logistics Management	402
Scope of Logistics Management	403
Transportation	404
Components of Transportation Network	404
Types of Transport Modes	404
Type of Transport – Summary	407
Transport provides	407
Common & Private Carriers	408
Freight Forwarders	408
Third Party Logistics (3PL) Providers	408
Advantages of 3PL providers	409
Disadvantages of 3PL providers	409
Factors for the Growth of 3PL providers	409
3PL Industry in India	410
Fourth Party Logistics Providers (4PL)	411
Stages of Fourth Party Logistics Solutions	411
Cost effectiveness of Fourth Party Logistics	411
Warehousing	412
Types of warehouses	412
Role of IT in warehousing	414
Advantages of IT warehousing	414
Warehouse Management Systems	415
Barriers to IT adoption in warehousing	416
Warehousing in India	417
Warehouse (Development and Regulation) Act, 2007	417
Logistics park	418
Free Trade Warehousing Zones (FTWZ)	418
Central Warehousing Corporation (CWC)	419
Inventory Management	420
Packaging	421
Containerisation/Unitization	422
Container	423

	Page
Types of Containers	423
Container Unit - 'Teu' Twentyfoot Equivalent Unit	425
Container Seal Numbers	425
Concepts of FCL & LCL	425
Procedure for Selection of the Container	425
Container Ship	426
Container Yard (CY)	426
Container Terminal	426
Sequence of Operations & Documentation Procedures in Container Terminal	426
Benefits of Containerisation	427
Containersation in India	427
Container Corporation of India Ltd.	427
Control and Communication	428
The Role Information Technology in Logistics	428
Emerging Trends in Application of IT for Logistics Management	430
LESSON ROUND UP	431
SELF-TEST QUESTIONS	432
TEST PAPERS	
Practice Test Paper	435

Lesson 1
Introduction to International Business

LESSON OUTLINE

- Business
- International business
- Drivers of international business
- Benefits of international business
- Scope of international business
- Difference between domestic and international business
- Globalization
- Meaning of globalisation
- Benefits of globalisation
- Criticisms of globalisation
- Myths about globalisation
- Risks in global business
- Issues in global business
- Globalisation and international trade
- Globalisation and financial markets
- Globalisation, income inequality, and poverty
- The future of globalisation
- Needs to go global
- Modes of entry and operation in International Business
- LESSON ROUND UP
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

Globalisation is the order of the day with most countries eliminating trade barriers and paving the way for growth and expansion of international business. During the last 15 years, world exports for goods have grown on average 6% a year. International business has become lifeline of every economy and country. For countries to flourish economically it is very important for them to encourage international business. The benefits of international business are immense. International business when undertaken with specific objectives by companies and promoted by governments of nations can lead to overall economic growth of the world at large. Every corporate and government has numerous and concrete reasons to take their business international. However it is necessary to keep in view various limitations of the globalisation also.

In this chapter we will learn about globalisation its positive and negative impacts and how globalisation of economy is taking place. There are different methods of entering foreign markets such as exporting, licensing, franchising, FDI, management contracts and turnkey projects. The choice of method of entry would depend on the long term corporate strategy taking into consideration various environmental factors in the host country and home country.

"Globalisation is creating rich countries with poor people."

Joseph Stiglitz

BUSINESS

A business is an economic activity related to continuous buying and selling of goods and services for satisfying human wants. A business is an organisation involved in the trade of goods and services or both to the consumers. Today's business carries a complex area of commerce and industries which includes the activities of both production and distribution of goods services. To the enterprises business is related with the decision. What to produce? When to produce? Whom to produce? Where to produce? How much to produce? In simplest word we can say that the modern time's business is very much complex. As the environment is dynamic and changes frequently so the above questions always make the business enterprises to rethink about their business strategies. Stephenson defines business as, "the regular production or purchase and sale of goods undertaken with the objective of earning profit and acquiring wealth through the satisfaction of human wants".

INTERNATIONAL BUSINESS

International business means the buying and selling of the goods and services across the border. These business activities may be of government or private enterprises. Here the national border are crossed by the enterprises to expand their business activities like manufacturing, mining, construction, agriculture, banking, insurance, health, education, transportation, communication and so on. A business enterprise who goes for international business has to take a very wide and long view before making any decision, it has to refer to social, political, historical, cultural, geographical, physical, ecological and economic aspects of the another country where it had to business. International business by its nature is a primary determinant of international trade, one of the results of the increasing success of international business ventures is globalization.

International Business is the process of focusing on the resources of the globe and objectives of the organisations on global business opportunities and threats. International business is defined as global trade of goods/services or investment.

DRIVERS OF INTERNATIONAL BUSINESS



1. Higher Rate of Profits: The basic objective of business is to achieve profits. When the domestic markets do not promise a higher rate of profits, business firms search for foreign markets where there is scope for higher rate of profits. Thus the objective of profit affects and motivates the business to expand operations to foreign countries. For example, Hewlett Packard in the USA earns more than half of its profits from the foreign markets as compared to that of domestic markets.

2. Expanding the Production Capacities beyond the Demand of the Domestic Country: Some of the domestic companies expand their production capacities more than the demand for the product in domestic countries. These companies, in such cases, are forced to sell their excess production in foreign developed countries. Toyota of Japan is an example.

3. Limited Home Market: When the size of the home market is limited either due to the smaller size of the population or due to lower purchasing power of the people or both, the companies internationalize their operations. For example, most of the Japanese automobiles and electronic firms entered the USA, Europe and even African markets due to smaller size of the home market. ITC entered the European market due to the lower purchasing power of the Indians with regard to high quality cigarettes.

4. Political Stability vs. Political Instability: Political stability does not simply mean that continuation of the same party in power, but it does mean that continuation of the same policies of the Government for a quite longer period. It is viewed that the USA is a politically stable country; countries like the UK, France, Germany, Italy and Japan are also politically stable. Most of the African countries and some of the Asian countries are politically instable countries. Business firms prefer to enter politically stable countries and are restrained from locating their business operations in politically instable countries. In fact, business firms shift their operations from politically instable countries to politically stable countries.

5. Availability of Technology and Competent Human Resources: Availability of advanced technology and competent human resources in some countries act as pulling factors for business firms from other countries. For example, American and European companies, in recent years, have been depended on Indian companies for software products and services through their business process outsourcing (BPO). This is because the cost of human resources in India is 10 to 15 times less compared to the US and European labour markets.

6. High Cost of Transportation: Initially companies enter foreign countries for their marketing operations. But the home companies in any country enjoy higher profit margins as compared to the foreign firms on account of the cost of transportation of the products. Under such conditions, the foreign companies are inclined to increase their profit margin by locating their manufacturing facilities in foreign countries through the Foreign Direct Investment (FDI) route to satisfy the demand of either one country or a group of neighbouring countries. For example, Mobil which was supplying petroleum products to Ethiopia, Kenya, Eritrea, Sudan etc., from its refineries in Saudi Arabia, established its refinery facilities in Eritrea in order to reduce the cost of transportation.

7. Availability of Raw Materials: The source of highly qualitative raw materials and bulk raw materials is a major factor for attracting the companies from various foreign countries. For example Vedanta Resources is a London Stock Exchange (LSE) listed UK based company operating principally in India due to availability of raw materials such as iron ore, copper, zinc and lead. It also has substantial operations in Zambia and Australia where ample copper is available.

8. Liberalisation and Globalisation: Most of the countries in the globe liberalized their economies and opened their countries to the rest of the globe. These change in policies attracted multinational companies to extend their operations to these countries.

9. Growth in Market Share: Some of the large-scale business firms would like to enhance their market share in the global market by expanding and intensifying their operations in various foreign countries. Smaller companies expand internationally for survival while the larger companies expand to increase their market share. For example Ball Corporation, the third largest beverage can manufacturer in the USA, bought the European packaging operations of Continental Can Company. Then it expanded its operations to Europe and met the European

demand which is 200 per cent more than that of the USA. Thus, it increased its global market share of soft drink cans.

BENEFITS OF INTERNATIONAL BUSINESS

High Living Standards	Increased Socio-Economic Welfare	Wider Market	Reduced Effects of Business Cycles
Reduced Risks	Large-scale Economies	Potential Untapped Market	Provides the Opportunity to Domestic Business
Division of Labour and Specialisation	Economic Growth of the World at large	Optimum and Proper Utilisation of World Resources	Cultural Transformation

1. High Living Standards: Comparative cost theory indicates that the countries which have the advantages of raw materials, human resources, natural resources and climatic conditions in producing particular goods can produce the products at low cost and also of high quality. Customers in various countries can buy more products with the same amount of money. In turn, it can also enhance the living standards of the people through enhanced purchasing power and by consuming high quality products.

2. Increased Socio-Economic Welfare: International business enhances consumption level, and economic welfare of the people of the trading countries. For example the people of China are now enjoying a variety of products of various countries like Coca-Cola, McDonald's range of products, electronic products of Japan and coffee from Brazil. Thus the Chinese consumption levels and socio-economic welfare has enhanced.

3. Wider Market: International business widens the market and increases the market size. Therefore, the companies need not depend on the demand for the product in a single country or customer's tastes and preferences of a single country. Due to the enhanced market Air France, now, mostly depends on the demand for air travel of the customers from countries other than France. This is true in case of most of the MNCs like Toyota, Honda, Xerox and Coca-Cola.

4. Reduced Effects of Business Cycles: The stages of business cycles vary from country to country. Therefore, MNCs shift from the country experiencing a recession to the country experiencing 'boom' conditions. This enables international firms to escape recessionary conditions.

5. Reduced Risks: Both commercial and political risks are reduced for the companies engaged in international business due to spread in different countries. Multinationals which were operating in erstwhile USSR were affected only partly due to their safer operations in other countries. But the domestic companies of the then USSR collapsed completely.

6. Large-scale Economies: Multinational companies due to wider and larger markets produce larger quantities, which provide the benefits of large-scale economies like reduced cost of production, availability of expertise, quality etc.

7. Potential Untapped Markets: International business provides the chance of exploring and exploiting the potential markets which are untapped so far. These markets provide the opportunity of selling the product at a higher price than in domestic markets. For example Bata sells shoes in the UK at £ 100 (around Rs. 8000) whose price is around Rs. 1200 in India.

8. Provides the Opportunity to Domestic Business: International Business firms provide opportunities to the domestic companies. These opportunities include technology, management expertise, market intelligence, product developments etc. For example Japanese firms like Honda, Yamaha, Suzuki and Kawasaki have combined to

form Joint Ventures with Indian companies to form Hero Honda, Birla Yamaha, Maruti Suzuki and Kawasaki Bajaj to share technology and product development expertise.

9. Division of Labour and Specialisation: International business leads to division of labour and specialization. For example Brazil specializes in coffee, Kenya in tea, Japan in automobiles and electronics, India in textile garments etc.

10. Economic Growth of the World at large: Specialization, division of labour, enhancement of productivity, posing challenges, development to meet them, innovations and creations to meet the competition lead to overall economic growth of the world nations. International business particularly helped the Asian countries like Japan, Taiwan, Korea, Philippines, Singapore, Malaysia and the United Arab Emirates.

11. Optimum and Proper Utilisation of World Resources: International business provides for the flow of raw materials, natural resources and human resources from the countries where they are in excess supply to those countries where they are in short supply or need most. For example flow of human resources from India, consumer goods from the UK, France, Italy and Germany to developing countries. This, in turn, helps in the optimum and proper utilization of world resources.

12. Cultural Transformation: International business benefits are not purely economical or commercial; they are even social and cultural. These days, we observe that the West is slowly tending towards the East and vice-versa. It does mean that the good cultural factors and values of the East are acquired by the West and vice-versa. Thus there is a close cultural transformation and integration.

SCOPE OF INTERNATIONAL BUSINESS

The scope of international business is much broader involving international marketing, international investments, management of foreign exchange, procuring international finance from International Monetary Fund (IMF), World Bank, International Finance Corporation (IFC), International Development Association (IDA) etc., management of international human resources, management of cultural diversity, management of international production and logistics, international strategic management and the like.

DIFFERENCE BETWEEN DOMESTIC AND INTERNATIONAL BUSINESS

Trade means exchange of goods and services for the satisfaction of human wants. The process of exchange includes purchase of goods and services and their sale. The trade may take place within geographical boundaries of countries or may be extended to across the border. When trade is confined to the geographical limits of a country, it is a domestic or national trade. In national trade both the buyer and the seller are of the same countries and they enter into trade-agreements subject to the national laws, practices and customs of trade. But International or foreign trade refers to the trade between two countries. Purchaser and seller are citizens of two different countries and are subject to International or bilateral laws of trade and tariffs. Technically, domestic trade and international trade are more or less identical and are based on the same basic principles of trades. There are certain similarities between domestic and international business in terms of broad objectives and goals of the company, namely:

- Generating revenue.
- Corporate image and brand building.
- Customer satisfaction and building loyalty as patronage buyers.
- Carrying out their operations by respecting and adhering to local regulations.
- Generation of employment opportunities.
- Both are subject to a set code of conduct and ethics which includes corporate governance.

But practically, there are certain differences between domestic and international business. It was on the basis of

these differences that the old classical economists propounded a separate theory for international trade. The main points of difference are as follows:

1. Environment: The economic, political, legal, socio-cultural, competitive and technology environments are well known in case of domestic business due to the familiarity of geography and place of operations, hence the organization can take the necessary precautions to assess its impact and adjust quickly to the changes in the same. In international operations the various aspects of the macro external environment are not fully known unless the business is established and created a place for itself in the market. Thus a number of innumerable hidden environmental factors may emerge during the settlement period which may pose problems. For example - an Indian company which wishes to enter and establish operations in the European markets may face numerous political, legal, socio-cultural and other problems cropping up in the external macro environment during the initial settlement stages. When fast food chain Mc Donald's entered India in 1996 had to ensure that it did not offer pork or beef items so as to gain acceptance locally. It also had to re-engineer its operations to address the special requirements of vegetarians in India and introduce variations in dishes that were not available at any Mc Donald's outlet anywhere in the world.

2. Plan and Strategy: Plans and strategies are generally worked out for the short term. The short term plans are linked together and carried forward into the long run. The inverse is also possible as domestic business offers the flexibility to organizations. In case of international business only a well thought out, proven, practical long term time-bound planning and strategy works.

3. Competition: The competitive forces operating in the domestic business environment are restricted to a local boundary. The movement of competitive forces can thus be analyzed and understood more clearly. In case of international business competitive forces are not restricted to a local boundary. They extend over several countries, thereby making it difficult to analyze their motive and movement.

4. Difference in Currencies: There is only one currency acceptable all over the country and therefore there are no difficulties in making payments in internal trade. But, each country has its own monetary system which differs from others. Exchange rates between the two currencies are fixed by the monetary authorities under the rules framed by the International Monetary Fund. All payments for imports are to be made in the exporting country's currency which is not freely available in importers country. The scarcity of foreign currency may sometimes limit the size of imports from other countries.

5. Tariffs and Quotas: The tariff rates and quotas imposed by various countries on their exports and imports do not directly and significantly influence domestic business operations. The international businesses are directly and significantly influenced by the tariff rates imposed by various countries. Also they have to operate within the quotas of exports and imports imposed by different countries.

6. Research and Development: It is reasonable and relatively simpler to carry out business product research, innovations, demand analysis and customer survey in domestic business. Also the reliability and success rate of their results are much higher. For e.g. Nestle Maggi has developed and introduced Vegetable Atta noodles, a variety of noodles which is available mostly only in India and not in other countries based on market research. Research and development in international business operations is expensive and difficult to conduct. Their reliability criteria depend on individual countries and there is no uniformity in the result of their applications. Quoting the same example Nestle Maggi has developed different varieties of noodles such as Kari Letup and Pizza which are particularly sold in Malaysia and Saudi Arabia and which may not be suitable to Indian markets.

7. Human Resources: Due to past successes, proven track record and established systems, business can prosper even if the human resources have minimum skills and knowledge. The task of human resources management is much simpler in domestic business. The international business requires multi-lingual, multi-strategic and multi-cultural human resources to handle varied risks spread over countries. Thus the task of human resource management is much more complex.

8. Organizational Vision and Objective: The organizational vision and objective in domestic business is narrowed

down to work in a single country with a steady growth objective. For e.g. a part of the vision of Tata Steel in 1998 – 99 was “In the coming decade, we will become the most competitive steel plant and so serve the community and the nation.” In case of international business the organizational vision and objective is more broadened to cover many countries and geographic and cultural diversity may influence the same. For e.g. the vision of Tata Steel Group’s vision currently states “We aspire to be the global steel industry benchmark for Value Creation and Corporate Citizenship”.

9. Investment: Depending on the size of domestic business operations one can start with a minimum investment. Involvement of regulatory bodies in respect of small local business enterprises is limited. On the other hand all overseas operations except exports, call for huge investments to set up and expand the business in many countries. Special regulatory bodies are involved in the process since foreign currency is transacted.

10. Distribution: Domestic business houses can use at its discretion to select any distribution channel to reach the customer. For e.g. small “Mom and Pop” stores are one of the most popular and widely used distribution channels for Fast Moving Consumer Goods (FMCG) in rural and urban India. The choice of distribution channel in international business operations is governed by the government or market practice of the nation where the business is operating. For e.g. cash and carry stores and shopping malls which are very commonly used channels in the developed markets are now catching up in urban India.

11. Logistics: Domestic business may involve use of conventional logistical methods engaging domestic players for procurement of raw materials and reaching of final products to the consumer. For e.g. carts and cycles are very commonly used means of transportation in the local Indian business operations even today. International business engages international players involving advanced technology and systems for effective logistical operations. For e.g. containerized transportation is the standard form of reaching the goods to the required destination in most developed nations.

12. Advertising and Promotion: Advertising, personal selling and other promotional methods are subject to the regulations prevailing in the domestic business operations. For e.g. advertisement and promotion of pharmaceutical drugs, cigarettes and alcohol are restricted in India. In case of international business different countries have different regulations with regard to advertisement and promotion. For e.g. advertisements of cigarettes and alcohol are permitted in some developed nations.

13. Approach: Domestic business’s approach is ethnocentric. It means that domestic companies formulate strategies, product design etc. towards national markets, customers and competitors. International business’s approach can be polycentric, regiocentric or geocentric. Under polycentric approach international business enters foreign markets by establishing foreign subsidiaries. Under region-centric approach, they export the product to the neighbouring countries of the host country. Under the geocentric approach, they treat the entire world as a single market for production, marketing, investment and drawing various inputs.

14. Difference in Natural and Geographical Conditions: Natural resources like availability of raw materials, composition of soil, fertility of soil, rainfall, temperature etc. differ widely from country to country. On the basis of this speciality, countries specialise themselves in the production of certain selected commodities and therefore they produce better quality of goods at lower rates and sell them in the international market. It causes difference in domestic trade and foreign trade.

15. Different Legal Systems: Different legal systems are operated by different countries and they all widely differ from each other. The existence of different legal systems makes the task of businessmen more difficult as they have to follow legal provisions of the two countries as regards the particular trade.

16. Mobility of Factors of Production: Mobility of different factors of production is less as between nations than in the country itself. However, with the advent of air transport, the mobility of labour has increased manifold. Similarly mobility of capital has increased with the development of international banking. Inspite of these developments, mobility of labour and capital is not as much as it is found within the country itself.

17. Sovereign Political Entities: Each country is an independent sovereign political entity. Different countries impose different types of restrictions on imports and exports in the national interest. The importers and exporters shall have to observe such restrictions while entering into agreement. These restrictions may be:

- Imposition of tariffs and customs duties on imports and exports;
- Quantitative restrictions like quota etc.
- Exchange control;
- Imposition of more local taxes etc.

No such restrictions are imposed on domestic trade or restrictions imposed on internal trade are quite different.

GLOBALISATION

Introduction

Globalisation is a more advanced form of internationalisation of business that implies a degree of functional integration between internationally dispersed economic activities. It denotes the increased freedom and capacity of individuals and firms to undertake economic transactions with residents of other countries. Globalisation is the process of international integration arising from the interchange of world views, products, ideas, and other aspects of culture. Globalisation refers to processes that promote world-wide exchanges of national and cultural resources. Advancement in transportation and telecommunications infrastructure, including the rise of the internet, has further catalysed globalisation of economic activities.

Several basic activities like investment (particularly foreign direct investment), the spread of technology, strong institutions, sound macroeconomic policies, an educated workforce, and the existence of a market economy leads to greater prosperity. There is substantial evidence, from countries of different sizes and different regions, that as countries "globalise" their citizens' benefit, in the form of access to a wider variety of goods and services, lower prices, more and better-paying jobs, improved health, and higher overall living standards. It is probably no mere coincidence that over the past 20 years, as a number of countries has become more open to global economic forces, the percentage of the developing world living in extreme poverty which is defined as living on less than $1 per day, has been cut in half.

Nike – A Global Company

Nike, the world's largest maker of athletic shoes, does not make any clothes or shoes itself. It contracts out production to South Korean and Taiwanese companies. These companies operate not only in their home countries but also in lower wage economies such as the Philippines and Vietnam. We source product from 715 factories, employing nearly 1 million workers across 44 countries as of August 2014. They do not own or operate any of these factories, except for 73 in-house manufacturing centers in the U.S. where they make patented parts.

Meaning of Globalisation

Globalisation refers to the increasing integration of economies around the world, particularly through the movement of goods, services, and capital across borders. The term sometimes also refers to the movement of people (labour) and knowledge (technology) across international borders.

The term "globalisation" began to be used more commonly in the 1980s, reflecting technological advances that made it easier and quicker to complete international transactions – both trade and financial flows. It refers to an extension of the same market forces that have operated for centuries at all levels of human economic activity – village markets, urban industries, or financial centres beyond national borders.

According to International Monetary Fund (IMF), globalisation means "the growing economic

interdependence of countries world wide through increasing volume and variety of cross-border transactions in goods and services and of international capital flows and also through the more rapid and widespread diffusion of technology".

Globalisation refers to the process of increasing economic integration and growing economic interdependence between nations. It means integration of different economies of the world into one global economy thereby reducing the economic gap between different countries. This is achieved by removing all restrictions on the movement of goods, services, capital, labour and technology by removing all restrictions on the movement of goods, services, capital, labour and technology between nations. Globalisation leads to an increased level of interaction and interdependence among different countries. There is free flow of goods, services, technology, management practices and culture across national boundaries. From a country's view point, globalisation means integration of the domestic economy of a country with the world economy.

In brief, globalisation implies being able to manufacture in the most cost-effective way possible anywhere in the world, being able to procure raw materials and management resources from the cheapest source anywhere in the world, and having the entire world as one market. The global corporations of today conduct their operations worldwide as if the entire world were a single entity. Globalisation also implies emergence of a world where innovation can arise anywhere in the world.

Globalisation also implies sharing of information and knowledge. Innovators in business or government can draw on ideas that have been successfully implemented in one jurisdiction and tailor them to suit their own jurisdiction. **Joseph Stiglitz, a Nobel laureate and frequent critic of globalisation, has nonetheless observed that globalisation "has reduced the sense of isolation felt in much of the developing world and has given many people in the developing world access to knowledge well beyond the reach of even the wealthiest in any country a century ago".**

The main features of globalisation

Reduction of trade barriers so as to ensure free flow of goods and services across national frontiers;	Creation of an environment in which free flow of capital can take place among nations;	Creation of an environment which permits free flow of technology between nations;	Creation of an environment in which free movement of labour can take place in different countries of the world; and	Creation of a global mechanism for the settlement of economic disputes between various countries.

Wimbledon Tennis Balls- Product of Globalised world

The Dunlop Slazenger balls used at Wimbledon (48,000) and many other major tennis tournaments are the product of materials and labour from at least 10 different countries.

The Dunlop Slazenger provided its first hand-sewn, wool-coated balls to Wimbledon in 1902. The Dunlop Slazenger factory is at Bataan on the island of Basilan in the southern Philippines. In the 1970s the Philippine government set up the Bataan Economic Zone in order to attract foreign investment. However, the economic zone never attracted the amount of investment initially hoped for and today much of it is derelict as companies have left for locations such as China where labour is even cheaper.

The main materials used for the manufacturing of tennis balls at the Bataan plant are:

- The rubber in the core of the ball comes from Malaysia, where it is delivered to a processing plant in

Prai, near Penang, from small rubber plantations in the area. The core of a ball is 40% rubber and 60% filler and chemicals.

- In addition rubber from Basilan is mixed with petroleum naphthalene to make glue for the balls.
- The greenish yellow cloth covering (wool and synthetic mix) is made in the UK at Dursley in Gloucestershire.
- The wool for the cloth is imported into the UK from New Zealand.
- The tins into which the balls are packed are from Indonesia. Among the substances used to vulcanise the rubber and give it the right amount of stretch and bounce are:
  - clay from South Carolina
  - sulphur from Korea
  - silica from Greece
  - magnesium carbonate from Japan
  - zinc oxide from Thailand.

BENEFITS OF GLOBALISATION

1. Increase in Competitive Strength of domestic industry: Globalisation exposes domestic industry in developing countries to foreign competition. This put domestic companies under pressure to improve efficiency and quality and reduce costs. Under a protective regime industry lose the urge to improve efficiency and quality. Globalisation helps to improve the competitive strength and economic growth of developing nations.

2. Access to Advanced Technology: For a developing country like India, globalisation provides access to new technology; Indian companies can acquire sophisticated technology through outright purchase or through joint ventures and other arrangements.

3. Access to Foreign Investment: Globalisation has attracted the much needed foreign capital towards developing countries like India. Foreign multinationals have invested billion of dollars in India. In addition, foreign institutional investors have brought in huge funds in stock markets in India.

4. Reduction in Cost of Production: In a globalised environment, companies can secure cheaper sources of raw materials and labour. For example, several foreign companies have set up BPOs and call centres in India due to lower cost of labour. Sometimes, a company may carry out its entire manufacturing in a foreign country to minimize cost of production.

5. Growth and Expansion: When the domestic market is not large enough to absorb the entire production, domestic companies can expand and grow by entering foreign markets. Japanese firms flooded the US markets with automobiles and electronics because of this reason. Companies from USA, Europe and other developed regions are increasing their presence in Asia due to growing population and increasing income levels in Asian countries.

6. Higher Volume of Trade: Due to globalisation, each country can specialize in the production of goods and services in which it has a comparative advantage. It can export its surplus output and import their items freely from other nations. This will lead not only to a phenomenal increase in the world trade but also to better allocation and utilization of resources in each country.

7. Consumer Welfare: Better quality and low priced goods and services will become available to consumers. This along with a wider choice in consumption will help improve standards of living of people in developing

countries. Over a period of time, the proportion of people below the poverty line will go down. Consumers also get access to products manufactured in any part of the world.

8. Other benefits: Globalisation also offers some spin off benefits. It helps in the professionalization of management. Globalisation brings people of different races and ethnic backgrounds closer. It helps to promote mutual cooperation and world peace.

CRITICISMS OF GLOBALISATION

1. Threat to Domestic Industry: Globalisation leads to increasing role of foreign companies in the domestic economy of a country. This is likely to hamper the growth of domestic companies. Small and medium firms in a developing country like India are not in a position to compete with giant firms of developed nations.

2. Unemployment: Globalisation brings about rapid technological changes. Advanced technology might create unemployment problems, particularly in developing country.

3. Threat to Democracy: Globalisation requires very fast movement of capital and labour across national frontiers. These increase the pressure for conceptual and structural readjustments to the breaking point. The social and human costs of globalisation may put the social fabric of a democracy in danger.

4. Economic Instability: Globalisation leads to a tremendous redistribution of economic power. Such redistribution will translate into a redistribution of political power. The change is likely to have a destabilizing effect.

5. Disregard of National Interest: A developing economy might become excessively dependent on global corporations. This may not be in the national interest.

MYTHS ABOUT GLOBALIZATION

1. Downward pressure on wages: It is generally believed that Globalisation is the primary factor that fosters wage moderation in low-skilled work conducted in developed countries. However, per the recent issue of the World Economic Outlook, a more significant factor is technology. As more work can be mechanized, and as fewer people are needed to do a given job than in the past, the demand for that labour falls, and as a result the wages for that labour is affected.

2. The "race to the bottom": Globalisation has not caused the world's multinational corporations to search of the lowest-paid labourers. There are numerous factors that enter into corporate decisions on where to source products, including the supply of skilled labour, economic and political stability, the local infrastructure, the quality of institutions, and the overall business climate. According to the UN Information Service, the developed world hosts two-thirds of the world's inward foreign direct investment. The 49 least developed countries – the poorest of the developing countries – account for around 2 per cent of the total inward FDI stock of developing countries. It is also not true that multinational corporations make a consistent practice of operating sweatshops in low-wage countries, with poor working conditions and substandard wages. Multinationals, on average, pay higher wages than what is standard in developing nations, and offer higher labor standards.

3. Globalisation is irreversible: In the long run, globalisation is likely to be an unrelenting phenomenon. But for significant periods of time, its momentum can be hindered by a variety of factors, ranging from political will to availability of infrastructure. Indeed, the world was thought to be on an irreversible path toward peace and prosperity early in the early 20th century, until the outbreak of Word War I. That war, coupled with the Great Depression, and then World War II, dramatically set back global economic integration. That fragility of nearly a century ago still exists today – as we saw in the aftermath of September 11th, when U.S. air travel came to a halt, financial markets shut down, and the economy weakened. The current turmoil in financial markets also poses great difficulty for the stability and reliability of those markets, as well as for the global economy. Credit market

strains have intensified and spread across asset classes and banks, precipitating a financial shock that many have characterized as the most serious since the 1930s. These episodes are reminders that a breakdown in globalisation – meaning a slowdown in the global flows of goods, services, capital, and people – can have extremely adverse consequences.

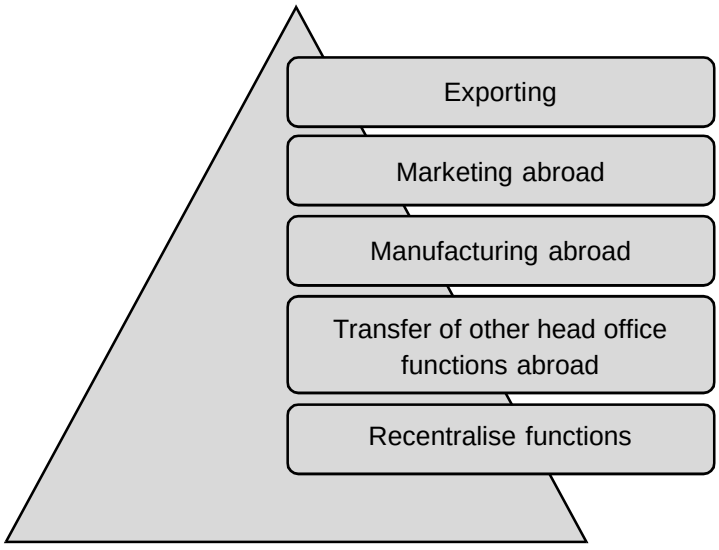
4. Openness to globalisation will, on its own, deliver economic growth: Integrating with the global economy is, necessary but not sufficient condition for economic growth. For globalisation to be able to work, a country cannot be saddled with problems endemic to many developing countries, from a corrupt political class, to poor infrastructure, and macroeconomic instability.

5. The shrinking state: Technologies that facilitate communication and commerce have curbed the power of some despots throughout the world, but in globalized world governments take on new importance in one critical respect, namely, setting, and enforcing, rules with respect to contracts and property rights. The potential of globalisation can never be realized unless there are rules and regulations in place, and individuals to enforce them. This gives economic actors confidence to engage in business transactions. Further undermining the idea of globalisation shrinking states is that states are not, in fact, shrinking. Public expenditures are, on average, as high or higher today as they have been at any point in recent memory. And among OECD countries, government tax revenue as a percentage of GDP increased from 25.5 percent in 1965 to 36.6 percent in 2000's.

STAGES OF GLOBALISATION

Normally, a firm passes through different stages of development before it becomes a truly global corporation. Typically, a domestic firm starts its international business by exporting. Later it may establish joint ventures or subsidiaries abroad. From an international firm it may then develop into a multinational firm and finally into a global one.

Kenichi Ohmae (1990) of McKinsey Japan identified five different stages in the development of a firm into a global corporation.



1st Stage: Exporting is the first stage and is also the least committed mode of entry into foreign markets. It is used by firms using an International or Global strategy where the local responsiveness is low. Domestic company moves into new markets overseas by linking up with local dealers and distributors.

2nd Stage: As a firm's commitment to a market increases it will move to the second stage and introduce some

marketing functions into country. This may now be associated with any of the other four modes, depending on the degree of commitment. It may also indicate that the firm is moving towards a multidomestic strategy.

3rd Stage: In the next stage, the domestic based company begins to carry out its own manufacturing in the key foreign markets. The licensing, joint venture or subsidiary mode may be used. It may indicate a move to a more multidomestic or global strategy from an International strategy, although many companies following an international strategy have manufacturing overseas, e.g. bulk pharmaceutical factories in Ireland.

4th Stage: The fourth stage of globalisation is the transfer of other head office functions to the subsidiaries. In stage four, the company moves to a full insider position in these markets, supported by a complete business system including R&D and engineering. This stage calls on the managers to replicate in a new environment the hardware, systems and operational approaches that have worked so well at home. It forces them to extend the reach of domestic headquarters, which now has to provide support functions such as personnel and finance, to all overseas activities. The transfer of R&D, engineering, finance etc. may end up forming a smaller clone of the head office, so-called insiderization. Many pharmaceutical and medical device subsidiaries in Ireland have reached this stage.

5th Stage: In the fifth stage, the company moves toward a genuinely global mode of operation. The fifth stage is to transfer functions back to the centre. The centre may not be the head office but a subsidiary that has shown a flair for a competence. This is similar to Ghoshal and Bartlett's (1989) transnational strategy. The functions transferred back may be human resources, finance functions from a shared service operation, R&D back to a small number of site to better exploit synergies, etc. There is some evidence that this is starting to occur, especially in competitive industries such as cars and microelectronics. There is some evidence of it occurring in the pharmaceutical industry. The recent large mergers are a symptom of this.

In this context Ohmae points out that a company's ability to serve local customers in markets around the globe in ways that are truly responsive to their needs as well as to the global character of its industry depends on its ability to strike a new organisational balance. What is called for is what Akio Morita of Sony has termed global localisation (glocalisation), a new orientation that simultaneously looks in both directions.

Getting to stage five, however, means venturing onto new ground altogether. Ohmae argues that to make this organisational transition, a company must denationalize their operations and create a system of values shared by corporate managers around the globe to replace the glue a nation based orientation once provided.

Ohmae further observes that today's global corporations are nationality less because consumers have become less nationalistic. True global corporations serve the interests of customers, not Governments. They do not exploit local situations and then repatriate all the profits back home, leaving each local area poorer for their having been there. They invest, they train, they pay taxes, they build up infrastructure and they provide good value to customers in all the countries where they do business. IBM Japan, for instance, has provided employment to about 20,000 Japanese and over the past decade has provided three times more tax revenue to the Japanese Government than has the Japanese company Fujitsu." Today many firms across the world have ambitious plans to become global.

RISKS IN GLOBAL BUSINESS

Global opportunities are not without risks – such as those arising from volatile capital movements. The International Monetary Fund works to help economies manage or reduce these risks, through economic analysis and policy advice and through technical assistance in areas such as macroeconomic policy, financial sector sustainability, and the exchange-rate system.

The risks are not a reason to reverse direction, but for all concerned – in developing and advanced countries, among both investors and recipients – to embrace policy changes to build strong economies and a stronger world financial system that will produce more rapid growth and ensure that poverty is reduced.

(i) **Political and Regulatory Risks:** Many countries of the world are not politically stable and transfer of political power does not happen in smooth ways in these countries. Therefore, companies doing business in these countries may have risk in new political regimes. Similarly, many countries have different types of regulations for doing business. Such regulations may be of quite different nature as compared to those prevailing in the domestic country. Therefore, the regulations of the host countries should be taken into account.

(ii) **Cultural and Managerial Risks:** Countries differ widely in terms of cultural characteristics like customer preferences and tastes, attitudes towards certain types of products/services, traditions, values and beliefs, and a host of other cultural factors. Therefore, products/services have to be tailored according to such requirements. Further, since management practices are culture-bound, the kinds of management practices which are effective in the domestic country may not be suitable in foreign countries. Therefore, there is a need for suitable change in management practices, more particularly related to human resource aspects.

(iii) **Exchange risk:** Every country has its own currency system as the currency of one country is not in circulation in the other country. Therefore, one currency is exchanged with another currency at some rate. The exchange rate keeps on fluctuating causing risk of loss to participants in international business

(iv) **Credit risk:** It is the risk of loss due to a debtor's non-payment of a loan or other line of credit (either the principal or interest (coupon) or both)It is difficult to ascertain the credit-worthiness of a foreign buyer. When a foreign buyer goes bankrupt, the domestic exporter faces great loss.

(v) **Transport risk:** Due to long distance between countries, goods are despatched by shipping or airways. Sea and transport are exposed to many types of additional risks.

(vi) **Market risk:** Competition in international business is severe and market conditions change frequently. It may not be possible for a firm to compete in international markets.

ISSUES IN GLOBAL BUSINESS

(i) Organisational Aspects: Resources can be allocated differently according to the treatment given to the organisation. A firm may establish a global financial system or it may treat foreign operations as a separate entity. In a unified system, excess cash in business units can be allocated by the management to the units that need money or to capital markets offering better returns. New capital can be available at the lowest cost. There are differences between countries in tax rates, freedom of remittances of profits, associated risks and so on; it is found generally beneficial to take larger share of profit from business in one place than another. A unified system has the ability to manage the currency exchange rates more readily and easily. These abilities can be motivating force for the strategists to go global. A global company can organise its activities on a global basis. But there are certain forces such as economic, culture, etc. and varying national interests that operate against a unified organizational systems.

(ii) Resource Allocation: Global companies are to raise capital and allocate them to domestic and foreign operations to support their strategies. In earlier years, it was a simple process of transferring the funds from the parent company to establish operations in foreign countries. Now-a-days, resource allocation is more complex because the financial and technological resources are available from host countries and international capital markets. Entry into foreign markets through licensing, franchising, joint ventures and subsidiaries are the orders of the day. It has become a complex process.

(iii) Leadership: Leadership styles vary according to the nations and hence a company wants to have business relation. A leadership style calling for specific skills and techniques may not work all the time in the countries. A leadership style effective in U.S.A may not be effective in China.

(iv) Plans and Policies: An organisation system has an impact on plans and policies for implementing a strategy involving global activities, in the areas of financé, marketing, research and development, operations.

In financial area, one has to face and manage fluctuating exchange rates, currency controls, quotas, tariff etc. Inflation, taxation and fiscal and monetary policies are influenced by the domestic and foreign government if the firm chooses to go global. Accounting principles and practices also vary from country to country. A unified financial system helps in easing these problems. In marketing area, the key issues is standardization of the product line across domestic and foreign markets. It relates product, prices, promotion and distribution variables. Research and development depends on how the firms take it. Countries are interested in bringing about faster economic process and welcome to build their own research calling for investment in this sector. A unified global research and development efforts allows spread of costs over a larger base as compared to research and development of national companies. However, responsiveness to local market conditions leads to the development of multiple research and development units. Production area, concerned with standardization to reduce costs and flexibility in management. An ideal strategy is one which is unified in which a limited number of factories of optimized scales of operation-choosing locations where material and labour costs are least. Instead of having entire production in one place, it pays to produce parts in one country and assemble in other parts.

GLOBALISATION AND INTERNATIONAL TRADE

A core element of globalisation is the expansion of world trade through the elimination or reduction of trade barriers, such as import tariffs. Greater imports offer consumers a wider variety of goods at lower prices, while providing strong incentives for domestic industries to remain competitive. Exports, often a source of economic growth for developing nations, stimulate job creation as industries sell beyond their borders. More generally, trade enhances national competitiveness by driving workers to focus on those vocations where they, and their country, have a competitive advantage. Trade promotes economic resilience and flexibility, as higher imports help to offset adverse domestic supply shocks. Greater openness can also stimulate foreign investment, which would be a source of employment for the local workforce and could bring along new technologies – thus promoting higher productivity.

Restricting international trade – that is, engaging in protectionism – generates adverse consequences for a country that undertakes such a policy. For example, tariffs raise the prices of imported goods, harming consumers, many of which may be poor. Protectionism also tends to reward concentrated, well-organized and politically-connected groups, at the expense of those whose interests may be more diffuse (such as consumers). It also reduces the variety of goods available and generates inefficiency by reducing competition and encouraging resources to flow into protected sectors.

Developing countries can benefit from an expansion in international trade. Ernesto Zedillo, the former president of Mexico, has observed that, "In every case where a poor nation has significantly overcome its poverty, this has been achieved while engaging in production for export markets and opening itself to the influx of foreign goods, investment, and technology." In the late 1980s, many developing countries began to dismantle their barriers to international trade, as a result of poor economic performance under protectionist polices and various economic crises. In the 1990s, many former Eastern bloc countries integrated into the global trading system and developing Asia – one of the most closed regions to trade in 1980 – progressively dismantled barriers to trade. Overall, while the average tariff rate applied by developing countries is higher than that applied by advanced countries, it has declined significantly over the last several decades.

GLOBALISATION AND FINANCIAL MARKETS

The world's financial markets have experienced a dramatic increase in globalisation in recent years. Global capital flows fluctuated between 2 and 6 percent of world GDP during the period 1980-95, but since then they have risen to more than tripling since 1995. The most rapid increase has been experienced by advanced economies, but emerging markets and developing countries have also become more financially integrated. As countries have strengthened their capital markets they have attracted more investment capital, which can enable

a broader entrepreneurial class to develop, facilitate a more efficient allocation of capital, encourage international risk sharing, and foster economic growth.

A recent paper by the IMF's Research Department takes stock of what is known about the effects of financial globalisation. The analysis of the past 30 years of data reveals two main lessons for countries to consider.

- First, the findings support the view that countries must carefully weigh the risks and benefits of unfettered capital flows. The evidence points to largely unambiguous gains from financial integration for advanced economies. In emerging and developing countries, certain factors are likely to influence the effect of financial globalisation on economic volatility and growth: countries with well-developed financial sectors, strong institutions, sounds macroeconomic policies, and substantial trade openness are more likely to gain from financial liberalization and less likely to risk increased macroeconomic volatility and to experience financial crises. For example, well-developed financial markets help moderate boom-bust cycles that can be triggered by surges and sudden stops in international capital flows, while strong domestic institutions and sound macroeconomic policies help attract "good" capital, such as portfolio equity flows and FDI.
- The second lesson to be drawn from the study is that there are also costs associated with being overly cautious about opening to capital flows. These costs include lower international trade, higher investment costs for firms, poorer economic incentives, and additional administrative/monitoring costs. Opening up to foreign investment may encourage changes in the domestic economy that eliminate these distortions and help foster growth.

Looking forward, the main policy lesson that can be drawn from these results is that capital account liberalization should be pursued as part of a broader reform package encompassing a country's macroeconomic policy framework, domestic financial system, and prudential regulation. Moreover, long-term, non-debt-creating flows, such as FDI, should be liberalized before short-term, debt-creating inflows. Countries should still weigh the possible risks involved in opening up to capital flows against the efficiency costs associated with controls, but under certain conditions (such as good institutions, sound domestic and foreign policies, and developed financial markets) the benefits from financial globalisation are likely to outweigh the risks.

GLOBALIZATION, INCOME INEQUALITY AND POVERTY

As some countries have embraced globalisation, and experienced significant income increases, other countries that have rejected globalisation, or embraced it only tepidly, have fallen behind. A similar phenomenon is at work within countries – some people have, inevitably, been bigger beneficiaries of globalisation than others.

Over the past two decades, income inequality has risen in most regions and countries. At the same time, per capita incomes have risen across virtually all regions for even the poorest segments of population, indicating that the poor are better off in an absolute sense during this phase of globalisation, although incomes for the relatively well off have increased at a faster pace. Consumption data from groups of developing countries reveal the striking inequality that exists between the richest and the poorest in populations across different regions. However, increased trade globalisation is not associated with a decline in inequality. The spread of technological advances and increased financial globalisation – and foreign direct investment in particular – have instead contributed more to the recent rise in inequality by raising the demand for skilled labor and increasing the returns to skills in both developed and developing countries.

It is important to ensure that the gains from globalisation are more broadly shared across the population. To this effect, reforms to strengthen education and training would help ensure that workers have the appropriate skills for the evolving global economy. Policies that broaden the access of finance to the poor would also help, as would further trade liberalization that boosts agricultural exports from developing countries. Additional programs may include providing adequate income support to cushion, but not obstruct, the process of change, and also making health care less dependent on continued employment and increasing the portability of pension benefits in some countries.

Globalisation should not be rejected because its impact has left some people unemployed. The dislocation may be a function of forces that have little to do with globalisation and more to do with inevitable technological progress. The number of people who "lose" under globalisation is likely to be outweighed by the number of people who "win".

Globalisation has helped to deliver extraordinary progress for people living in developing nations. Globalisation has contributed to a reduction in poverty as well as a reduction in global income inequality. Higher growth rates in globalizing developing countries have translated into higher incomes for the poor.

Secretary-General of the United Nations, Kofi Annan pointed out that "the main losers in today's very unequal world are not those who are too much exposed to globalisation. They are those who have been left out."

As individuals and institutions work to raise living standards throughout the world, it will be critically important to create a climate that enables these countries to realize maximum benefits from globalisation. That means focusing on macroeconomic stability, transparency in government, a sound legal system, modern infrastructure, quality education, and a deregulated economy.

As much as has been achieved in connection with globalisation, there is much more to be done. Regional disparities persist: while poverty fell in East and South Asia, it actually rose in sub-Saharan Africa. The UN's Human Development Report notes there are still around 1 billion people surviving on less than $1 per day – with 2.6 billion living on less than $2 per day. Proponents of globalisation argue that this is not because of too much globalisation, but rather too little. And the biggest threat to continuing to raise living standards throughout the world is not that globalisation will succeed but that it will fail. It is the people of developing economies who have the greatest need for globalisation, as it provides them with the opportunities that come with being part of the world economy.

GLOBALISATION AND STRATEGIC MANAGEMENT

The 1990s witnessed dramatic changes in the dynamics of global and national market places. These changes produced variety of outcomes and still continue to shape the business landscape in the twenty first century. All these changes and the resultant outcomes brought strategic management at the core of the corporate management irrespective of their location or scope of operation. The role of strategic management is to identify opportunities and threats in the external environment and use organizational strengths and weaknesses either to reap these opportunities or to meet the challenges. The rate of this change is accelerating day by day and so the tools and techniques of strategic management are increasingly being used to respond to these changes and inherent dynamics of external environment. A key to understand the role of strategic management is to have some perspective and understanding of the forces of this change.

The concept of global market place has taken on new meaning for all enterprises (small, medium and large) and for individual consumers. Changes in the government policies and the new technologies have made the global economy concept a fact of life. Presently every organization has to operate with a global perspective because either its operations have crossed the national boundaries or it is facing competition from global players in its domestic market. Now most businesses are not only buying and selling globally but using global alternatives and complex networks in their operations.

Globalisation has offered opportunities to gain new customers overseas, to achieve lower costs through overseas operations, and to achieve economies of scale. Global business can be undertaken through exports, licensing of products in favour of overseas partners, franchising functional subsidiaries, partly/wholly-owned subsidiaries, and joint ventures. Indian organizations are using all these avenues in varying proportion.

Strategies for global business differ from those for domestic business because of difference in the nature of competitive forces. A firm's decision to adopt strategies for global business depends on two factors:

(i) extent of cost pressures to denote the demand on a firm to minimize its per unit costs; and

(ii) extent of pressures for local responsiveness to denote to make a firm to tailor its strategies to respond to national-level differences in terms of variables like customer preferences and tastes, government policies, and business practices.

Often, these two factors are contradictory as minimizing costs may not be possible when products/services are to be differentiated. The juxtaposition of these two factors results in the following four types of strategies for global business:

(i) Global Strategy: In global strategy, assumptions are made that customer needs are similar worldwide. It is argued that markets are converging and increasingly people's needs and desires have homogenized. Therefore, firms can sell standardized products in the same way everywhere, for example, steel, pharmaceuticals, cement, petroleum, etc. When given a choice between a low-priced standard product and a high-priced nationally customized product, many customers will go for low-priced product. Thus, firms offering standardized products globally have competitive advantage in the form of lower costs resulting from economies of scale in product development, production and marketing. In contrast, distinct markets mean incurring additional costs in most of value chain activities.

***(ii) International Strategy*:** In the initial stages of globalisation, a firm may not be in a position to opt for either global strategy or multidomestic strategy for its overseas business. They adopt international strategy which involves creating an international division and exporting the products through that division to those countries where the products are needed. At this stage of globalisation, a company is really focused on the domestic market and just exporting what is demanded abroad. As the product becomes successful abroad, the company may set-up manufacturing and marketing facilities with certain degree of differentiation based on product customization. The key characteristic of this strategy is that all control is retained at the home office regarding product and marketing functions. Many multinational corporations have adopted this procedure.

(iii) Multidomestic Strategy: In multidomestic strategy, companies try to achieve a high level of local responsiveness by making their product/service offerings to the requirements of the countries they operate in. In this case, multidomestic companies attempt to extensively customize their products/services according to the local conditions operating in different countries. It is noted that some of the products may be standardized worldwide, but a majority of products cannot be. Customers' preferences and tastes are quite different in many countries for different products, for example, food products, garments etc. Similarly, differences exist in other areas too like infrastructure, distribution channels, government rules and regulations, etc. For meeting the requirements of all these conditions, customized products are needed. Hence, multidomestic strategy is essentially based on differentiation of the products.

(iv) Transnational Strategy: Transnational strategy involves adopting a combined approach of low costs and high local responsiveness simultaneously by the companies for their products/services. Integrating these two contradictory approaches is a difficult proposition and requires innovative ways.

THE FUTURE OF GLOBALIZATION

Globalisation seems to be gathering more and more momentum. The world is made up of nation states and a global marketplace. We need to get the right rules in place so the global system is more resilient, more beneficial, and more legitimate. International institutions have a difficult but indispensable role in helping to bring more of globalisation's benefits to more people throughout the world. By helping to break down barriers – ranging from the regulatory to the cultural – more countries can be integrated into the global economy, and more people can seize more of the benefits of globalisation

GLOBALISATION OF INDIA

India opened up the economy in the early nineties following a major crisis led by a foreign exchange crunch that dragged the economy close to defaulting on loans. The response was a slew of domestic and external sector policy measures partly prompted by the immediate needs and partly by the demand of the multilateral

organisations. The new policy regime radically pushed forward in favour of a more open and market oriented economy. Major measures initiated as a part of the liberalisation and globalisation strategy in the early nineties included scrapping of the industrial licensing regime, reduction in the number of areas reserved for the public sector, amendment of the monopolies and the restrictive trade practices act, start of the privatisation programme, reduction in tariff rates and change over to market determined exchange rates.

Over the years there has been a steady liberalisation of the current account transactions, more and more sectors opened up for foreign direct investments and portfolio investments facilitating entry of foreign investors in telecom, roads, ports, airports, insurance and other major sectors. However, many multi-national corporations even today remark that doing business in India is difficult. Discuss some of the favourable factors and obstacles to globalisation in India.

Hints:

1. The favourable factors for globalisation of Indian business are-

   - ***Human Resources:*** India has one of the largest pools of scientific and technical manpower. The number of management graduates is also surging. It is widely recognised that given the right environment, Indian scientists and technical personnel can do excellently. Cheap labour has particular attraction for several industries.
   - ***Wide Base:*** India has a very broad resource and industrial base which can support a variety of businesses.
   - ***Growing Entrepreneurship:*** Many of the established industries are planning to go international in a big way. Added to this is the considerable growth of new and dynamic entrepreneurs who could make a significant contribution to the globalisation of Indian business.
   - ***Growing Domestic Market:*** The growing domestic market enables the Indian companies to consolidate their position and to gain more strength to make foray into the foreign market or to expand their foreign business.
   - ***Niche Markets:*** There are many marketing opportunities abroad present in the form of market niches. (A niche is a small segment of a market ignored or not properly served by large players). Such niches are particularly attractive for small companies. Several Indian companies have become very successful by niche marking.
   - ***Expanding Markets:*** The growing population and disposable income and the resultant expanding internal market provide enormous business opportunities.
   - ***NRIs:*** The large number of non-resident Indians who are resourceful - in terms of capital, skill, experience, exposure, ideas etc., is an asset which can contribute to the globalisation of Indian business. The contribution of the overseas Chinese to the recent impressive industrial development of China may be noted here.
   - ***Economic Liberalisation:*** The economic liberalisation in India is an encouraging factor of globalisation. The de-licensing of industries, removal of restrictions on growth, opening up of industries earlier reserved for the public sector, import liberalisations, liberalisation of policy towards foreign capital and technology etc., could encourage globalisation of Indian business. Further, liberalisation in other countries increases the foreign business opportunities for Indian business.
   - ***Competition:*** The growing competition, both from within the country and abroad, provokes many Indian companies to look, to foreign markets seriously to improve their competitive position and to increase the business. Sometimes companies enter foreign market as a counter - competitive strategy, i.e., fight the foreign company in its own home market to weaken its competitive strength.

2. Some of the obstacles to globalisation in India are as follows-

- ***Government Policy and Procedures:*** Government policy and procedures in India are among the most complex, confusing and cumbersome in the world. Even after the much publicised liberalisation, they do not present a very conducive situation. One prerequisite for success in globalisation is swift and efficient action. Government policy and the bureaucratic culture in India in this respect are not that encouraging.
- ***High Cost:*** High cost of many vital inputs and other factors like raw materials and intermediates, power, finance infrastructural facilities like port etc., tend to reduce the international competitiveness of the Indian business.
- ***Poor Infrastructure:*** Infrastructure in India is generally inadequate and inefficient and therefore very costly. This is a serious problem affecting the growth as well as competitiveness.
- Obsolescence: The technology employed, mode and style of operations etc., are, in general, obsolete and these seriously, affect the competitiveness.
- ***Resistance to Change:*** There are several socio-political factors which resist change and this comes in the way of modernisation, rationalisation and efficiency improvement. Technological modernisation is resisted due to fear of unemployment. The extent of excess labour employed by the Indian industry is alarming. Because of this labour productivity is very low and this in some cases more than offsets the advantages of cheap labour.
- ***Poor Quality Image:*** Due to various reasons, the quality of many Indian products is poor. Even when the quality is good, the poor quality image India has becomes a handicap.
- ***Supply Problems:*** Due to various reasons like low production capacity, shortages of raw materials and infrastructures like power and port facilities, Indian companies in many instances are not able to accept large orders or to keep up delivery schedules.
- ***Small Size:*** Because of the small size and the low level of resources, in many cases Indian firms are not able to compete with the giants of other countries. Even the largest of the Indian companies are small compared to the multinational giants.
- ***Lack of Experience:*** The general lack of experience in managing international business is another important problem.
- ***Limited R & D and Marketing Research:*** Marketing Research and R & D in other areas are vital inputs for development of international business. However, these are poor in Indian business
- ***Growing Competition:*** The competition is growing not only from the firms in the developed" countries but also from the developing country firms. Indeed, the growing competition from the developing country firms is a serious challenge to India's international business.
- ***Trade Barriers:*** Although the tariff barriers to trade have been progressively reduced thanks to the GATT/WTO, the non-tariff barriers have been increasing, particularly in the developed countries. Further, the trading "blocs like the NAFTA, EC etc., could also adversely affect India's business.

NEEDS TO GO GLOBAL

All organizations irrespective of whether they are small or medium or large, are keen to enter into international business. Established companies are expanding their business. Many countries encourage trade, and removal of strangulating trade barriers motivates companies to aggressively multiply their targets. The governments of various countries are also determined to make their economy grow through international business, which has therefore become an inevitable part of their economic policy. The motive behind international business can be looked at:

A. From an individual company's viewpoint

B. From the government's viewpoint

From an individual company's viewpoint

1. Managing the product life cycle: All companies have products which pass through different stages of their lifecycles. After the product reaches the last stage of the cycle called the declining stage in on country, it is important for the company to identify a few other countries where the whole life cycle stages could be encased. For example, Enfield India reached maturity and the declining stage in India for the 350cc Royal Enfield motorcycle. The company entered Kenya, West Indies, Mauritius and other destinations where the heavy engine two wheeler became popular. The Suzuki 800cc vehicle reached the last stage of its life cycle in Japan, and entered India in the early 1980s, where it is still doing good business.

2. Geographic expansion as a growth strategy: Even if companies expand their business at home, they may still look overseas for new markets and better prospects. For example, Arvind Mills expanded their business by either setting up units or opening warehouses abroad. Ranbaxy's growth is mainly attributed to geographic expansion every year to new territories.

3. The adventurous spirit of younger generation in the organization: The younger generation of business families have considerable international exposure. They are willing to take risks and challenges and also create opportunities for their business. For example Kumar Mangalam Birla of the Aditya Vikram Birla Group of companies has managed to establish their business operations in several countries across the globe in the last decade.

4. Corporate ambition: Every corporate in the country has strategic plans to multiply its sales turnover. In case some of the ventures fail, others will offset the losses because of multi-locational operations. For example Coca cola is not doing well in a number of countries including India. But this will not affect the company because more than a hundred countries are contributing to offset the losses.

5. Technology advantage: Some companies have outstanding technology through which they enjoy core competencies. There is a need for such technology in all the countries. Biocon, Infosys and Tata Consultancy are known for their core competencies in biotechnology and software development respectively and a huge demand exists across many developed economies of the world for their technology.

6. Building a corporate image: Prior to profits and revenue generation, many companies first build their corporate image abroad. Once the image is built up, generating revenue is a comparatively easy task. For example LG Electronics and Samsung Electronics built their image in India during the initial three to five years after their entry and generation of revenues and profits has been considerable as they have expanded to semi-urban and rural India overtaking traditional Indian brands Godrej and Videocon.

7. Incentives and business impact: Companies, which are involved in international business, enjoy fiscal, physical and infrastructural incentives while they set up business in the host country. The Adtiya Vikram Birla group enjoyed such incentives in Thailand and Indonesia. The home country may also offer many incentives in order to neutralize the cost and allow the country to compete in the world market. For example recently the Prime Minister of Bangladesh Sheikh Hasina invited Indian companies to invest in proposed Special Economic Zones (SEZ) offering infrastructure facilities and tax holidays to such Indian companies.

8. Labour advantage: Many companies have a highly productive labour force. The unique skills may not be available throughout the world. Manufacturing units in India have consistently performed well, whether in the diamond industry (E.g. Surat) or automobile manufacturing (E.g. Hyundai Motor car manufacturing plant near Chennai). Companies nurture the skills of such labour force and win world markets.

9. New business opportunities: Many companies have entered into businesses abroad, seeing unlimited opportunities. For example health care companies like Cipla, Dr. Reddys Laboratories and Auronindo Pharma have entered into South American countries like Brazil and Argentina looking at the attractive business opportunities in such countries.

From the governments viewpoint

1. Earning valuable foreign exchange: Foreign exchange is necessary to balance the payments for imports. India imports crude oil, defence equipment, essential raw materials and medical equipment for which the payments have to be made in foreign exchange. If the exports are greater than imports it indicates a surplus in the balance of payments, on the other hand if the imports are higher and the exports are lower as has always been the case with India it indicates an adverse balance of payment.

2. Interdependency of nations: From time immemorial, nations have mutually depended on each other. Even during of Indus Valley civilization, Egypt and the Indus Valley depended on each other for various items. Today India depends on the Gulf regions for crude oil and in turns the Gulf region depends on India for rice, tea etc. Developed countries depend on developing countries for primary good, whereas developing countries depend on developed countries for value added finished products.

3. Trade theories and their impact: The theories of absolute advantage, comparative advantage and competitive advantage, which have been propounded by classical economists, indicate that a few nations have cost advantages in procurement of resources and production of finished products than other nations. Such advantages enable them to be competitive. These resources may be in the form of labour, infrastructure, technology, natural resources or even a proactive policy of the government. For example falling land prices in the South American countries of Paraguay and Uruguay has thrown open a tremendous opportunity for India edible oil companies to venture into offshore oilseeds cultivation with the industry representative body Solvent Extractor's Association (SEA) negotiating with ICICI Bank for a Rs. 150 Crore loan to part the proposed investment in the project.

4. Diplomatic relations: Diplomacy and trade always go hand in hand. Many sovereign nations send their diplomatic representatives to other countries with a motive of promoting trade besides maintaining cordial relations. Indian diplomats in Latin America have done a remarkable job of promoting India's business in the 1990s. However Pakistan being a failed nation has not been much successful in this endeavour.

5. Core competency of nations: Many countries are endowed with resources, which are produced at an optimum level. Such countries can compete well anywhere in the world. Rubber products from Malaysia, knitwear from India, rice from Thailand and wool from Australia are a few illustrations.

6. Investment for infrastructure: Over the years all countries have invested huge amounts of money on infrastructure by building airports, sea ports, economic zones and inland container terminals. If the trade activities do not increase and flourish, the country cannot recover the amounts invested. Hence, the government fixes targets for every infrastructure unit and time frame to achieve them. Economies like Mauritius, Hong Kong, Singapore, Malta and Cyprus invest in trade related infrastructure in order to elevate themselves to be foreign trade oriented economies.

7. National image: A new era has emerged from conquering countries by sword to winning by trade. A businessman gives priority to the image of the country he belongs to. We come across products with labels such as 'Made in Japan', 'Made in China' and 'Made in India'. Businessmen from Japan, China and India endeavor to make their products world class and bring credentials to their country while citizens achieve business success elsewhere in the world.

8. Foreign trade policy: All developing countries announce their foreign trade policies. A clear cut road map is drafted and given to promotional bodies so that timely implementation is possible. For instance the Commerce and Industry ministry Mr Anand Sharma has assured that the Government of India would extend its support to the slowdown hit export sector by providing more sops in the Foreign Trade Policy (FTP) to be unveiled next month at a conference organized by the industry body Federation of Indian Chambers of Commerce and Industry (FICCI). He said that the FTP would be a mix of fiscal incentives and simplification of procedures for carrying out foreign trade.

9. WTO and international agencies: The apex body of world trade, the World Trade Organization (WTO), a free, transparent and regulatory body upholds provisions related to elimination or reduction of tariff and non-tariff barriers. The International Bank for Reconstruction and Development (IBRD), popularly called the World Bank extends financial assistance on a soft loan basis in order to assist developing countries in their infrastructure

and industrial development. The International Monetary Fund (IMF) maintains currency stability in various countries through regulatory mechanisms. Many more organizations like International Maritime Organization, International Standard Organization, International Telecommunication Union, and International Civil Aviation Organization are major catalysts to promote trade between nations.

MODES OF ENTRY AND OPERATION IN INTERNATIONAL BUSINESS

Walmart's Entry through the World – Case study

Walmart which became an international company in 1991 today operates in over 11,000 retail units under 71 banners in 27 countries and e-commerce websites in 10 countries. Let us have a look at how Walmart became internationally successfully.

Mexico: Walmart entered Mexico through a joint venture with the leading retailer in 50:50 partnership. They soon acquired the partner completely. Walmart is all about local economies of scale, local purchasing power and local logistics. So what Walmart sells in Canada, over 85% of it is sourced from Canada. Walmart follows the logic that local scale and local market power determine the cost structure, branding and retail presence in eyes of customer. In the 1990s when Walmart opened its first store in Mexico, they had a huge American-style parking lot. They found all the shopping carts were piled at far end of parking lot – because customers came in via buses not cars. They made mistakes in terms of the product mix. They were selling the same thing as in the US. There was a story about them selling golf balls to customers whose income levels were low. The mistakes they made in Mexico were relatively early and non-fatal. They recovered from them very quickly. That was really the first non-US foray so they were learning on the fly. Today Mexico is a fantastic story for Walmart.

Argentina: Walmart entered Argentina in 1995 by setting up 100%-owned greenfield stores. They were pretty tiny by 2007 and had only 13 stores. Argentina is a small economy compared to Mexico. In 2007, according to a Citigroup report, Walmart's market share of organized retail was 4% and the combined market share of the two biggest players was 22%. Walmart acquired Central American Retail Holdings Company in 2007 and became No. 1 company in Argentina including Costa Rica, Guatemala, Honduras, Nicaragua as the acquired company had operations in all these economies. These are small markets, not strategically critical. But from Day One Walmart was No. 1 in these markets because the acquired businesses were already No 1. They were already adapted to the local economy and there was a high degree of localization.

Hong Kong: Hong Kong was their first foray into Asia. It was a brief disaster. Walmart knew nothing about Asia. They entered Hong Kong through a joint venture with a Thai conglomerate. This was unwise because instead of picking a Taiwanese or Hong Kong company as a local partner, they picked a Thai partner. They opened three stores and shut them down very quickly. Hong Kong is a very compact place and they didn't factor in how customers would get to the stores. There was nothing wrong with the product mix. They did not factor in the broader ecosystem – how customers will come and go. They chose a very inconvenient location for customers. It shows that Walmart from time to time, hasn't been the smartest company in terms of joint venture partners.

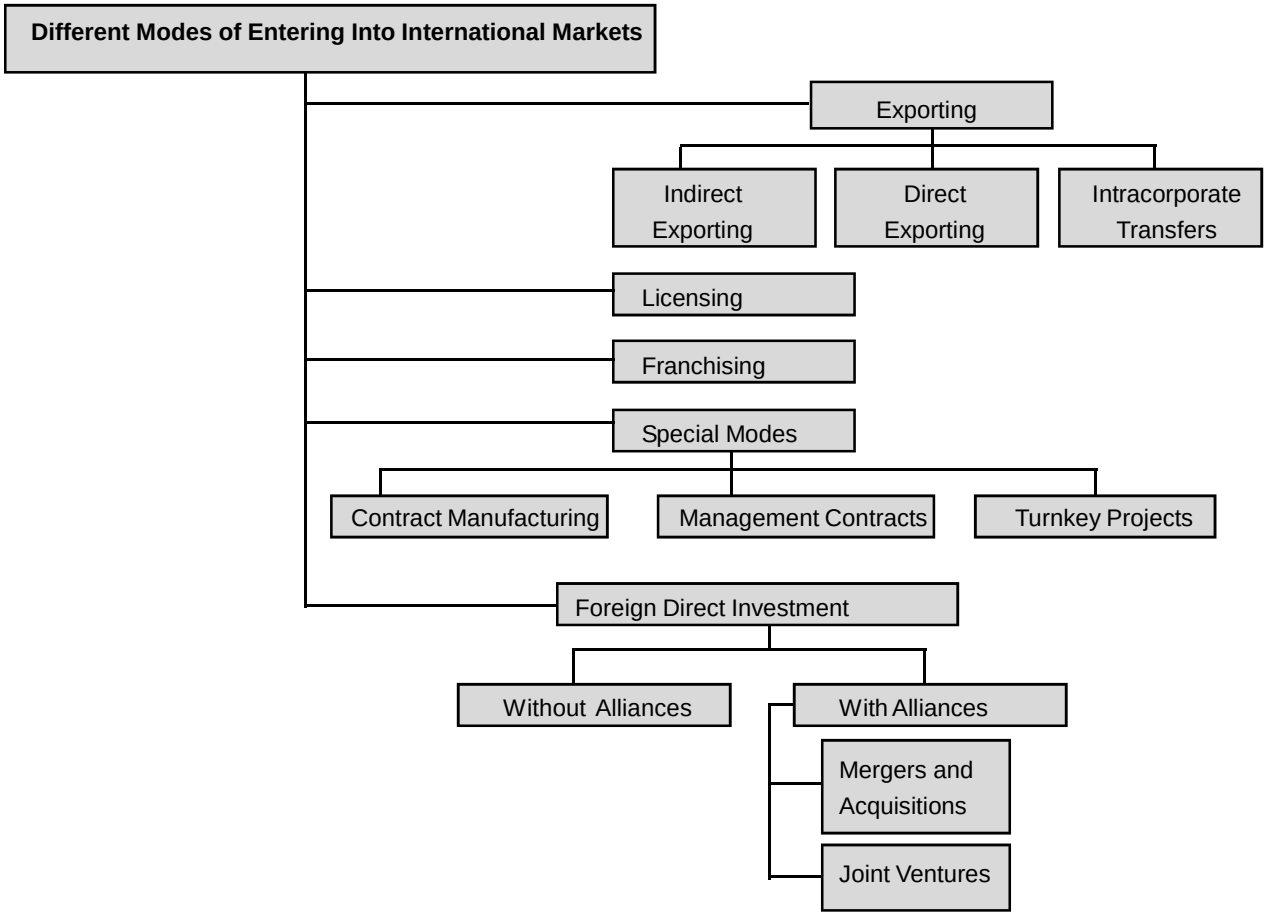
Indonesia: When Walmart entered to Indonesia there was political unrest. They entered via a non-equity route – there was no money in the agreement with the Lippo group. There were riots in Indonesia and the store was burnt down. Walmart didn't own or run the store. So it was not so much of an issue. The agreement with Lippo fell apart.

Korea: Walmart entered Korea in 1999. They entered by acquiring four units from Macro (a Dutch chain, now owned by Metro). Korea is fairly mature market and there was a local company called Emart, which is the market leader. Emart warned Walmart that this is a very local industry and it doesn't matter that you are the biggest retailer in the world – we are the biggest retailer in Korea. Walmart made an acquisition offer to Emart which Emart rejected. Walmart entered as a small player and could never become big. Seven years later they sold their stores to Emart and got out.

China: Walmart is still too early in the game in China. It's a respected retailer in China. They do a good job in terms of localization of the product mix and store format. There have been no big mistakes. Carrefour entered at roughly same time as Walmart – but its growing faster, it has double of the number of stores and is much more profitable

than Walmart. Walmart appears to be looking at China as one big national market – the same way it views the US. Carrefour looks at China as a portfolio of regional/local markets. Unlike Carefour Walmart has centralised sourcing and a centralised distribution centre. Carrefour gives greater autonomy to store managers. It is not even relying on local economies of scale, forget global. China's infrastructure is better than India's but it is in the process of being built up – when you have weak infrastructure for consumer goods, you have national manufacturers and not local manufacturers. In terms of food products, Chinese like to buy fresh meat so local sourcing is much smarter than centralised sourcing. Just like any developing economy, heterogeneity across China in terms of what people want to buy is very high. Carrefour can open one store in the middle of the city and tell the local store manager you are an independent profit manager – so you decide what you want to buy, from whom. Your competitor is the small mom and pop store in the city. It's a perfectly fine strategy. In retailing, local government bureaus become very important so if you give store managers high degree of autonomy it makes it easy for them to understand how to work with local governments. Carrefour is looking at China as a portfolio of local markets.

India: Walmart formed partnership in India with Bharti Enterprises in 2007. The joint venture's purpose was to build and operate cash and carry superstores in India under the name Best Price Modern Wholesale. As partners, the two companies jointly built 20 superstores. But the partnership failed and broke in 2013. When you enter a new market, a lot depends on the kind of a partner you have. If you have a partner that itself has ambitions to be a major retail powerhouse in India, there is a strategic conflict. Sooner or later India will permit foreign retailers to have direct equity ownership in India. Bharti has retail ambitions – it will want to buy Walmart's shares then, rather than sell. If stores are branded BestPrice, what is Walmart getting in this deal? One could argue that Walmart should have thought of India as a portfolio of regional markets and work with smaller regional partners. It's hard for them to have much bargaining power or have national ambitions. They would have been happy to brand them as Walmart and when regulations change, Walmart would be able to buy them out. So there was strategic failure on the part of Walmart to enter India.



EXPORTING

Exporting is the easiest and most widely used mode of entering in international markets. Exporters can be classified in various ways as given below.

1. Small or Large exporters: Depending upon the size of the business, exporters are classified as small or large exporters. Current foreign trade policy in India provides incentives and facilities to promote both small exporters and large exporters who are status holders due to their performance in earning foreign exchange.

2. Single or Multi-product exporters: Depending upon the product lines exported, they are classified as single product or multi product exporters.

3. Depending upon the legal status, exporters are classified as proprietary companies, partnership companies, private limited companies and public limited companies.

4. Depending upon the destination of exports, they are exporters as single destination exporters or multi destination exporters. Nowadays, the majority of companies adopt the philosophy of multi product, multi locational, multi strategic and multi dimensional operations.

5. Depending upon the frequency of exports, exporters are classified as occasional exporters and dynamic exporters.

Exporting includes indirect exporting, direct exporting and intra-corporate transfers.

(1) Indirect Exporting

Indirect exporting is exporting the products either in their original form or in the modified form to a foreign country through another domestic company. It is the market entry technique which offers lowest risk & least market control. The firm is not engaged in international marketing and no special activity is carried on within the firm. The sale is handled just like domestic sales. For example – various publishers in India like Himalaya Publishing House sell their products to UBS publishers of India, which in turn exports these books to various foreign countries.

(2) Direct Exporting

Direct exporting is selling the products to a country directly through its distribution arrangement or through a host country's company. For example : Baskin Robins initially exported its ice-cream to Russia in 1990 and later opened 74 outlets with Russian partners. Finally in 1995 it established its ice cream plant in Moscow.

(3) Intra-corporate Transfers

Intracorporate transfers means selling of product; by a company to its affiliated company in host country (another country). For example selling of products by Hindustan Lever in India to Unilever in USA This transaction is treated as exports in India and imports in USA.

Some of the factors to be considered by a company while exporting are as follows:

- Government policies like export policies, import policies, export financing, foreign exchange.
- Marketing factors like image, distribution networks, responsiveness to the customer, customer awareness and customer preferences
- Location consideration: These factors include physical distribution costs, warehousing costs, transportation costs, inventory carrying costs etc.

LICENSING

Licensing is the method of foreign operation whereby a firm in one country agrees to permit a company in

another country to use the manufacturing, processing, trademark, know-how or some other skill provided by the licensor. Coca Cola is an excellent example of licensing. In Zimbabwe, United Bottlers have the license to make Coke. In return the licensee produces the licensor's products, market these products in his assigned territory and pay the licensor loyalties related to the sales volume of the products. International licensing is an agreement between the licensor and the licensee over a period of time for the use of brand name, marketing knowhow, copyright, work method, and trade mark by paying a licence fee. For example, British American tobacco company (BATS) has given licenses in many countries for the manufacture of their brand of cigarettes "555". In India, ITC is the licensed producer of "555". Pepsi cola granted license to Heineken of the Netherlands giving them the exclusive right to produce and sell Pepsi cola in the Netherlands. The licensor has minimum involvement in day to day functions. Therefore, the returns are also comparatively low. The domestic company can choose any international location and enjoy the advantages without incurring any obligations and responsibilities of ownership, managerial, investment etc.

Licensing gives the following advantages:

- Good way to start in foreign operations and open the door to low risk manufacturing relationships
- It brings new technology and know-how in the licensees' country.
- Linkage of parent and receiving partner interests means both get most out of marketing effort
- Capital not tied up in foreign operation and Options to buy into partner exist or provision to take royalties in stock.

Some of the disadvantages of licensing are as follows:

- Limited form of participation - to length of agreement, specific product, process or trademark;
- Potential returns from marketing and manufacturing may be lost;
- Partner develops know-how and so licence is short;
- Licensees become competitors as once know-how is transferred, there is a risk that the foreign firm may act on its own.
- Requires considerable fact finding, planning, investigation and interpretation.

FRANCHISING

Franchising refers to the methods of practicing and using another person's business philosophy. The franchisor grants the independent operator the right to distribute its products, techniques, and trademarks for a percentage of gross monthly sales and a royalty fee. Various tangibles and intangibles such as national or international advertising, training, and other support services are commonly made available by the franchisor. Agreements may typically last from five to thirty years. A business for which franchising is said to work best have the following characteristics:

- Businesses with a good track record of profitability.
- Businesses built around a unique or unusual concept.
- Businesses with broad geographic appeal.
- Businesses which are relatively easy to operate.
- Businesses which are relatively inexpensive to operate.
- Businesses which are easily duplicated.

***Franchisor*:** Selects franchisee and provides franchisor the services of operating systems, receives the fixed

amount trade marks, product reputations and royalty from the & support systems like franchisee for providing the advertising, employee training, expertise and brand quality assurance programmes reputations to franchisee etc.

***Franchisee*:** An independent organization, agrees to follow franchisor's requirement like appearance, operating procedures, financial reporting, customer service under a franchising agreement. Some Pays a fixed amount and flexibility allowed under the royalty based on the sales to agreement the franchisor

Advantages For franchisors

- ***Expansion*:** Franchising is one of the only means available to access venture investment capital without the need to give up control of the operation of the chain in the process. After the brand and formula are carefully designed and properly executed, franchisors are able to sell franchises and expand rapidly across countries and continents using the capital and resources of their franchisees, and can earn profits commensurate with their contribution to those societies while greatly reducing the risk and expense that would be inherent in conventional chain operations.
- ***Legal considerations*:** The franchisor is relieved of many of the mundane duties necessary to start a new outlet, such as obtaining the necessary licenses and permits. In some jurisdictions, certain permits (especially alcohol licenses) are more easily obtained by locally based, owner-operator type applicants while companies based outside the jurisdiction (and especially if they originate in another country) find it difficult if not impossible to get such licences issued to them directly. For this reason, hotel and restaurant chains that sell alcohol often have no viable option but to franchise if they wish to expand to another state or province.
- ***Operational considerations*:** Franchisees are said to have a greater incentive than direct employees to operate their businesses successfully because they have a direct stake in the start up of the branded business and the tangible assets that wear the brand name. The need of franchisors to closely scrutinize the day to day operations of franchisees (compared to directly-owned outlets) is greatly reduced.

Advantages for franchisees

- ***Employment*:** As practiced in retailing, franchising offers franchisees the advantage of starting up a new business quickly based on a proven trademark and formula of doing business, as opposed to having to build a new business and brand from scratch (often in the face of aggressive competition from franchise operators).
- ***Expansion*:** With the help of the expertise provided by the franchisors, the franchisees may be able to take their franchised businesses to a level which they wouldn't have been able to without the expert guidance of their franchisors.
- ***Training*:** Franchisors often offer franchisees significant training, which is not available for free to individuals starting their own business. Although training is not free for franchisees, it is sometimes supported through the traditional franchise fee that the franchisor collects and tailored to the business that is being started. When training fees and travel expenses, etc. are required beyond the initial franchise fee, these fees are deductible as part of the start-up expenses of the business.

Disadvantages for franchisors

- ***Control*:** Successful franchising necessitates a much more careful vetting process when evaluating the limited number of potential franchisees than would be required in the hiring of direct employees who may have experience in the concept sector. An incompetent manager of a directly-owned outlet can easily be replaced, while, regardless of the local laws and agreements in place, removing an incompetent franchisee who owns the tangible assets of the business is much more difficult. Incompetent franchisees

can easily damage the public's goodwill towards the franchisor's brand by providing inferior goods and services. If a franchisee is cited for legal violations, (s)he will probably face the legal consequences alone but the franchisor's reputation could still be damaged.

– ***Limited pool of viable franchisees*:** In any city or region there may be only a limited pool of prospects who have both the financial resources and the desire to purchase and start up a franchised business, as compared to the pool of individuals who can be hired and trained to competently manage directly-owned businesses, as paid employees. However, in periods of recession where traditional good jobs are in short supply, this disadvantage disappears because those who can't find good jobs are willing to invest money in a franchise as a means of self-employment.

Disadvantages for franchisees

– ***No guarantee*:** usually, there is a guarantee of financial success for the franchisee made by the franchisor in the written disclosure circular and the actual franchise agreement. While the estimated start-up costs of the franchise are an implied "earnings claim" some businesses do fail, including franchised outlets. Unfortunately, the unit financial performance statistics are not required to be disclosed to new buyers of franchises and this omission makes it impossible for new buyers of franchises to assess the odds of success and failure of their investment in the franchise in terms of profitability and failure as experienced on a unit basis of the franchise system.

– ***Control*:** For franchisees, the main disadvantage of franchising is a loss of control. While they gain the use of a system, trademarks, assistance, training, marketing, the franchisee is required to follow the system and get approval for changes from the franchisor. For these reasons, franchisees and entrepreneurs are very different.

– ***Price*:** Starting and operating a franchise business carries expenses. In choosing to adopt the standards set by the franchisor, the franchisee often has no further choice as to signage, shop fitting, uniforms etc. The franchisee may not be allowed to source less expensive alternatives. Added to that is the franchise fee and ongoing royalties and advertising contributions. The contract may also bind the franchisee to such alterations as demanded by the franchisor from time to time.

– ***Conflicts*:** The franchisor/franchisee relationship can easily cause conflict if either side is incompetent (or acting in bad faith). An incompetent franchisor can destroy its franchisees by failing to promote the brand properly or by squeezing them too aggressively for profits. Franchise agreements are unilateral contracts or contracts of adhesion wherein the contract terms generally are advantageous to the franchisor when there is conflict in the relationship.

SPECIAL MODES

These have special strategies and include contract manufacturing, management contracts and turnkey projects:

Contract Manufacturing

Contract manufacturing is a process that established a working agreement between two companies. As part of the agreement, one company will custom produce parts or other materials on behalf of their client. In most cases, the manufacturer will also handle the ordering and shipment processes for the client. As a result, the client does not have to maintain manufacturing facilities, purchase raw materials, or hire labor in order to produce the finished goods. The basic working model used by contract manufacturers translates well into many different industries. Since the process is essentially outsourcing production to a partner who will privately brand the end product, there are a number of different business ventures that can make use of a contract manufacturing arrangement. There are a number of examples of pharmaceutical contract manufacturing currently functioning today, as well as similar arrangements in food manufacturing, the creation of computer components and other forms of electronic contract manufacturing. Even industries like personal care and hygiene products, automotive

parts, and medical supplies are often created under the terms of a contract manufacture agreement. There are several advantages to a contract manufacturing arrangement. For the manufacturer, there is the guarantee of steady work. Having contracts in place that commit to certain levels of production for one, two and even five year periods makes it much easier to forecast the future financial stability of the company. For the client, there is no need to purchase or rent production facilities, buy equipment, purchase raw materials, or hire and train employees to produce the goods. There are also no headaches from dealing with employees who fail to report to work, equipment that breaks down, or any of the other minor details that any manufacturing company must face daily. All the client has to do is generate sales, forward orders to the manufacturer, and keep accurate records of all income and expenses associated with the business venture.

Management Contracts

A management contract is an arrangement under which operational control of an enterprise is vested by contract in a separate enterprise which performs the necessary managerial functions in return for a fee. Management contracts involve not just selling a method of doing things (as with franchising or licensing) but involves actually doing them. A management contract can involve a wide range of functions, such as technical operation of a production facility, management of personnel, accounting, marketing services and training. Management contracts have been used to a wide extent in the airline industry, and when foreign government action restricts other entry methods. Management contracts are often formed where there is a lack of local skills to run a project. It is an alternative to foreign direct investment as it does not involve as high risk and can yield higher returns for the company.

Turnkey Projects

Turn-key refers to something that is ready for immediate use, generally used in the sale or supply of goods or services. The term is common in the construction industry, for instance, in which it refers to the bundling of materials and labour by sub-contractors. A "turnkey" job by a plumber would include the parts (toilets, tub, faucets, pipes, etc.) as well as the plumber's labour, without any contribution by the general contractors. This is commonly used in motorsports to describe a car being sold with drive train (engine, transmission, etc.) as a racer may prefer to keep the pieces to use in another vehicle to preserve a combination. Similarly, this term may be used to advertise the sale of an established business, including all the equipment necessary to run it, or by a business-to-business supplier providing complete packages for business start-up. In a turnkey business transaction, different entities are responsible for setting up a plant or equipment (e.g. trains/infrastructure) and for putting it into operation. It can include contractual actions - at least through the system, subsystem, or equipment installation phase. It may also include follow-on contractual actions, such as testing, training, logistical, and operational support. It is often given to the best bidder in a procurement process. Turnkey projects can also be extended, known as turnkey plus, where there is perhaps a small equity interest by the supplier and it will later on continue its operation through a management contract or licensing. Turnkey is often used to describe a home built ready for the customer to move in. If a contractor builds a "turnkey home" they frame the structure and finish the interior. Everything is completed down to the cabinets and carpet.

FOREIGN DIRECT INVESTMENT WITHOUT ALLIANCES

Some companies enter the foreign markets through exporting, licensing, franchising etc., get the knowledge and awareness of the foreign markets, culture of the country, customers' preferences, political situation of the country etc and then establish manufacturing facilities by ownership in the foreign countries. Baskin Robbin's in Russia followed this strategy. In this arrangement, the internationl firm makes a direct investment in a production unit in a foreign market. It requires greatest commitment since there is 100% ownership. It is also called the Greenfield investment. The parent company starts a new venture in a foreign country by constructing new operational facilities from the ground up. In addition to building new facilities, most parent companies also create new long-term jobs in the foreign country by hiring new employees. Green field investments occur when

multinational corporations enter into developing countries to build new factories and/or stores. Developing countries often offer prospective companies tax-breaks, subsidies and other types of incentives to set up green field investments. Governments often see that losing corporate tax revenue is a small price to pay if jobs are created and knowledge and technology is gained to boost the country's human capital.

FOREIGN DIRECT INVESTMENT WITH STRATEGIC ALLIANCES

Innovations, creations, productivity, growth, expansions and diversifications in recent years are mostly accomplished by strategic alliances adopted by various companies. Strategic alliances are a co-operative approach to achieve the larger goals. Strategic alliances can take different forms like licensing, franchising, contract manufacturing, JVs etc. Alliances are a strategy to explore a new market which the companies individually cannot do. Example: Xerox of USA and Fuji of Japan collaborated to explore new markets in Europe and Pacific Rim

Mergers and Acquisitions

International mergers and acquisitions are growing day by day. These mergers and acquisitions refer to those mergers and acquisitions that are taking place beyond the boundaries of a particular country. International mergers and acquisitions are also termed as global mergers and acquisitions or cross-border mergers and acquisitions. Globalisation and worldwide financial reforms have collectively contributed towards the development of international mergers and acquisitions to a substantial extent. International mergers and acquisitions are taking place in different forms, for example horizontal mergers, vertical mergers, conglomerate mergers, congeneric mergers, reverse mergers, dilutive mergers, accretive mergers and others. International mergers and acquisitions are performed for the purpose of obtaining some strategic benefits in the markets of a particular country. With the help of international mergers and acquisitions, multinational corporations can enjoy a number of advantages, which include economies of scale and market dominance. International mergers and acquisitions play an important role behind the growth of a company. These deals or transactions help a large number of companies penetrate into new markets fast and attain economies of scale. They also stimulate foreign direct investment or FDI. The reputed international mergers and acquisitions agencies also provide educational programs and training in order to grow the expertise of the merger and acquisition professionals working in the global merger and acquisitions sector. The rules and regulations regarding international mergers and acquisitions keep on changing constantly and it is mandatory that the parties to international mergers and acquisitions get themselves updated with the various amendments. Numerous investment bank professionals, consultants and attorneys are there to offer valuable and knowledgeable recommendations to the merger and acquisition clients.

Joint venture

A Joint Venture is an entity formed between two or more parties to undertake economic activity together. The parties agree to create a new entity to share in the revenues, expenses, and control of the enterprise. Joint ventures can be defined as "an enterprise in which two or more investors share ownership and control over property rights and operation". The venture can be for one specific project only, or a continuing business relationship. Entering into a joint venture is a major decision. Businesses of any size can use joint ventures to strengthen long-term relationships or to collaborate on short-term projects.

CASE STUDY - ENTRY STRATEGIES OF STARBUCKS

Starbucks' history began in Seattle in 1971, when three students named Jerry Baldwin, Zev Siegel, and Gordon Bowker decided to be partners and opened a little shop in Pike Place Market to sell high-quality coffee beans and equipment. They were influenced by a trip to Africa where they tried a huge variety of coffee flavours.

In 1981, Howard Schultz, Vice President and General Manager of U.S. Operations for Hammarplast, noticed Starbucks' success and decided to analyze the company in more depth. He was struck by the business

philosophy of serving good coffee with dark roasted flavour profiles. He wanted to transmit that coffee passion by working for the Starbucks enterprise to expand outside Seattle, thereby exposing people all over America to Starbucks coffee. However, the founders were against hiring him because geographic expansion was too risky and because they did not share Schultz's vision for Starbucks. Finally, they reconsidered Schultz's idea and decided to hire him as head of Marketing.

After that, Schultz was trained about Starbucks' coffee culture and then was sent to Italy to attend an international house wares show. In Italy, he visited a variety of coffee bars and noticed that Starbucks needed to serve fresh-brewed coffee, espresso, and cappuccino in its stores in addition to beans and coffee equipment. Besides, he considered that Starbucks stores would be a place to meet friends as they would at home. Re-creating the Italian coffee-bar culture in the United States could be Starbucks' differentiating factor.

Baldwin and Bowker were not interested in serving coffee. They regarded that to expand their business would deviate from their core business. They were however attracted by the idea to acquire Peet's Coffee and Tea, which took place in 1984.

Finally they decided to give Schultz the opportunity to test an espresso bar. Howard Schultz was convinced that his idea was a big winner. He eventually left Starbucks to start his own business, called Il Giornale in 1985. In 1987, Schultz raised enough capital with local investors and purchased Starbucks. He first combined Starbucks and Il Giornale operations, and then re-branded both businesses under the Starbucks name. He wanted Starbucks to become the most respected brand name in coffee and to be admired for its corporate social responsibility, its values and its guiding principles.

Today Starbucks is the largest coffee shop company in the world. It is specialized in high quality of coffee which derives one hundred percent from the Arabic coffee variety. Starbucks is characterized by its "third place concept". A coffee company seeks its customers to consider its stores as a place between home and work. Moreover, its success owes to its introducing a new way to drink coffee and its coffee culture. At present Starbucks has more than 15,700 stores in 43 countries. It is becoming one of the most respected brands in the world. Starbucks uses different entry modes in its internationalization process. Starbucks adapts its international strategy in order to satisfy the needs and requirements of every market, seeking to respect its cultures and traditions.

At present, the company uses three different strategies: joint venture, licenses and wholly–owned subsidiaries.

Before entering a new country Starbucks conducts rigorous quantitative market studies. The company also develops extensive focus group interviews to get a pulse of the marketplace and potential. Starbucks has demonstrated that even a large company needs help to achieve its goals. In order to succeed, a company needs to realize that it often cannot alone fill the gap in serving the needs of its target market. Starbucks has mostly entered into strategic partnership to enter new markets and obtain the products and services available in that market quickly. Strategic partnerships have enhanced Starbucks' competitiveness in the marketplace. They have also helped the company to keep pace with the rapid changes of technological innovation. Starbucks was able to achieve its objectives, break into new markets, and enhance its bottom line by entering into strategic alliances with the right companies.

Starbucks has certain criteria for consideration of 'International Partners'. They seek to ensure their local partners will share its value and commitment to bringing the Starbucks Experience to customers worldwide. Those selection criteria may include the following: a partner who shares its values and corporate culture; a partner with a strategic fit to Starbucks' business; a seasoned operator of small-box, multi-uni retail stores; a local business leader; someone with a strong track record developing new ventures; someone with experience managing licensed & premium brands and concepts; and a partner with food & beverage experience. Further selection criteria include sufficient financial and human resources, and involvement and commitment with top management. A final point is the partner's real estate knowledge and access to leverage their structure.

Starbucks has developed the following procedure of global expansion: The Company selects local partners

who are local business leader. Then, Starbucks together with its partner try to adapt its business traditions to the local market. For instance, Starbucks coffee stores in Spain have outside terraces, and in Japan coffee shops have more seats than others countries and provide a smaller serving.

Starbucks' involvement in the internationalization process varies only in degree (e.g. licensing, joint venture and wholly-owned subsidiary) since the company is constantly in touch with operators to keep abreast of the marketplace. In a joint-venture, Starbucks' equity position varies across a wide range. Lately, the company tends to minimize its holding and requires a local partner (as in the Spain case) to hold most of the capital cost (Isidro 2004). Starbucks holds less than 50% of the shares in their joint ventures. Schultz commented that Starbucks is constantly attracting potential partners.

Starbucks in United Kingdom

Starbucks Coffee Company Ltd (UK) is a wholly-owned subsidiary of Starbucks Corporation of the US, which is the world's largest retailer and roaster of specialist coffee. It is the market leader of branded coffee shops in the UK.

In May 1998, Starbucks entered into the UK by the acquisition of sixty-five Seattle Coffee Company stores. It acquired the Seattle Coffee Company in exchange for about 1.8 million shares of common Starbucks stock, or about £50.8 million. Starbucks re-branded the purchased Seattle Coffee stores in the year following their purchase.

Seattle Coffee Company was founded in 1995. It included the Seattle's Best Coffee and Torrefazione Italia Coffee brands (Coffeegeek 2003). The company was managed by two Americans, Scott and Ally Svenson. Seattle Coffee Company opened its first coffee bar in Covent Garden in 1996. As of 1998 it had sixty-five retail stores selling American style coffee which has a similar coffee culture as Starbucks.

Entering the UK was a milestone for Starbucks' international expansion. The internationalization plan in Starbucks' long-term strategy consisted of opening 500 retail stores in Europe by the end of 2003. "We are a way from taking the step from the U.K. to Europe," said Schultz, Chairman and Chief Executive Officer of Starbucks (Holmes 1998). What's more, Schultz said Europe was a "major strategic opportunity to achieve our goal of creating and building an enduring global brand" (Holmes 1998).

The low competition intensity in earlier times drove Starbucks to expand in a strategically smart way, which was to create and build a sustainable brand. In the UK Starbucks has grown step by step until becoming recognized as one of the "Top 10 UK Best Places to Work" in 2007 (Starbucks Homepage 2008). In 1999, Starbucks formed an alliance with Sainsbury's. Starbucks also acquired London coffee shops from Madison's Coffee for £1.4 million in 2001. In 2002, Starbucks formed a partnership with Borders bookshops and bought 13 coffee bars from Coffee Republic for £2 million. By early 2005, Starbucks had 30 concessions in supermarkets. In 2006, Starbucks UK was listed as one of "UK Top 50 Best Places to Work" (ranked 34th), awarded by the Great Places to Work Institute, in partnership with the Financial Times.

Howard Behar, President of Starbucks Coffee International said "We do not believe we are an American company, but an international brand. We hope to benefit from the pub culture in the UK to make Starbucks a natural meeting place for people". The above remark intends to reduce the importance of cultural distance between Starbucks' coffee concept and United Kingdom's coffee concept. Between the two countries, there was a huge gap. British people had a different way of thinking than Americans. In the United Kingdom, there was also certain opposition to American products and concepts. Starbucks sought to reduce that distance by acquiring an existing British coffee chain, Seattle Coffee stores. In addition, Starbucks waited a year to re-brand the acquired Seattle Coffee stores with the Starbucks brand. In this way, Starbucks first made the British familiar with the Starbucks Coffee concept prior to rebranding.

In 2007, Starbucks gained a major success in the UK with more than 500 stores having been opened. It remained the most recognized chain coffee store, with 27% of the respondents rating it their favourite (with Costa at 15%). As of the present moment, Starbucks has more than 600 branches in the UK and Ireland.

According to the retail analyst Euromonitor, the company has a 16.7 per cent market share, one per cent ahead of Costa Coffee. Costa Coffee is founded in 1971 by Italian brothers Vilas Costa with a wholesale operation supplying roasted coffee. Besides, it is based in United Kingdom.

In view of the facts and circumstances given in the case above, analyse the following:

1. Discuss the partner selection criteria of Starbucks and analyse it with the with reference to partner in UK.
2. Which entry mode strategy did Starbucks used to enter United Kingdom and why?

Hints:

1. Starbucks has certain criteria for consideration of 'International Partners'. They seek to ensure their local partners will share its value and commitment to bringing the Starbucks Experience to customers worldwide. Those selection criteria may include the following: a partner who shares its values and corporate culture; a partner with a strategic fit to Starbucks' business; a seasoned operator of small-box, multi-uni retail stores; a local business leader; someone with a strong track record developing new ventures; someone with experience managing licensed & premium brands and concepts; and a partner with food & beverage experience. Further selection criteria include sufficient financial and human resources, and involvement and commitment with top management. A final point is the partner's real estate knowledge and access to leverage their structure.
2. Starbucks has developed the following procedure of global expansion: The Company selects local partners who are local business leader. Then, Starbucks together with its partner try to adapt its business traditions to the local market. For instance, Starbucks coffee stores in Spain have outside terraces, and in Japan coffee shops have more seats than others countries and provide a smaller serving. Starbucks' involvement in the internationalization process varies only in degree (e.g. licensing, joint venture and wholly-owned subsidiary) since the company is constantly in touch with operators to keep abreast of the marketplace. In a joint-venture, Starbucks' equity position varies across a wide range.

LESSON ROUND UP

- International business means the buying and selling of the goods and services across the border.
- Globalisation is a more advanced form of internationalization of business that implies a degree of functional integration between internationally dispersed economic activities. The term sometimes also refers to the movement of people (labour) and knowledge (technology) across international borders.
- Globalisation leads to an increased level of interaction and interdependence among different countries.
- A firm passes through different stages of development before it becomes a truly global corporation. Typically, a domestic firm starts its international business by exporting. Later it may establish joint ventures or subsidiaries abroad. From an international firm it may then develop into a multinational firm and finally into a global one.
- A core element of globalisation is the expansion of world trade through the elimination or reduction of trade barriers, such as import tariffs.
- Exporting is the easiest and most widely used mode of entering in international markets. Licensing is the method of foreign operation whereby a firm in one country agrees to permit a company in another country to use the manufacturing, processing, trademark, know-how or some other skill provided by the licensor. Coca Cola is an excellent example of licensing.
- Franchising refers to the methods of practicing and using another person's business philosophy. The

franchisor grants the independent operator the right to distribute its products, techniques, and trademarks for a percentage of gross monthly sales and a royalty fee.

- A management contract is an arrangement under which operational control of an enterprise is vested by contract in a separate enterprise which performs the necessary managerial functions in return for a fee.
- Contract manufacturing is a process that established a working agreement between two companies.
- Greenfeild investment is a form of foreign direct investment where a parent company starts a new venture in a foreign country by constructing new operational facilities from the ground up. In addition to building new facilities, most parent companies also create new long-term jobs in the foreign country by hiring new employees.

SELF TEST QUESTIONS

1. What is international business? Differentiate between domestic and international business.
2. Examine the impact of globalisation on financial markets citing some recent data and statistics.
3. Has globalisation led to increase in inequality and poverty? Critically examine.
4. Explain the different stages of globalisation.
5. Discuss the problems and prospects of globalisation of Indian business.
6. Examine the pros and cons of globalisation with special reference to India.
7. Explain different modes of entry in international trade with examples.
8. What are the drivers of international trade? explain.
9. Discuss the risks and issues in global business.
10. Describe the objectives of international business.

Lesson 2
International Business Environment

LESSON OUTLINE

- Concept of international business environment
- Economic environment
- Technological environment
- Political & legal environment
- Socio-cultural environment
- Global environment
- Physical environment
- Tools for environmental analysis
  - PEST analysis
  - SWOT analysis
  - Porter's five forces model
  - Global Competitiveness Index
- LESSON ROUND UP
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

The global business environment is highly dynamic. The trade barriers are falling very much in international business. The number of countries in international trade has more than tripled in the past 50 years. During the last 15 years, world exports for goods have grown on average 6% a year. Businesses find themselves dealing with more individual countries, each with their own economic, political, technological commercial environment and legal systems. Today, there are variety of international trade rules and practices.

In today's scenarios operating in global environment means getting affected by activities around the world in all the sectors. International business environment is highly complex and changing rapidly. Organisations need to assess the environment carefully in order to survive and prosper their businesses.

In this chapter we will discuss about the business environment in global perspective and some tools to assess the international business environment.

"Business environment is the aggregate of all conditions, events and influences that surround and affect business."

David Keith

BUSINESS ENVIRONMENT

Environment literally means the surrounding, external objects, influences, or circumstances under which someone or something exists. Davis Keith defines the environment of business as “the aggregate of all conditions, events and influences that surround and affect it.”

There are two sets of factors- internal and external – which influence the business policy of an organization. The internal factors are known as controllable factors because the organization has control over these factors. The business can modify or alter such factor to suit the environment. The external factors are known as uncontrollable factors and legally beyond the control of the individual enterprise.

The internal environment consists of a large number of factors which contribute to the success or failure of an organization. It refers to all the factors within an organisation, which impart strength or create weaknesses of a strategic nature. Strength is an inherent capacity of an organisation which can be used to gain strategic advantage over its competitors. On the other hand, the weakness of an organisation refers to its inherent limitation or constraint which creates a strategic disadvantage. Some of the important internal factors include organisational resources, research and development and technology capabilities, financial capabilities, marketing capabilities, operations capabilities etc.

The term “business environment” generally refers to the external forces, factors and institutions that are beyond the control of the business and they affect the functioning of a business enterprise and include factors outside the firm which can lead to opportunities for or threats to the firm. Although there are many external factors, the most important factors include customers, competitors, suppliers, government, and the social, political, legal and technological factors etc.

While some of these factors or forces may have direct influence over the business firm, others may operate indirectly. Thus, business environment may be defined as the total surroundings, which have a direct or indirect bearing on the functioning of business. It may also be defined as the set of external factors, such as economic factors, social factors, political and legal factors, demographic factors, and technical factors etc., which are uncontrollable in nature and affects the business decisions of a firm.

The success of every business depends on adapting itself to the environment within which it functions. The business has to make the necessary changes to adapt it to the new policies. Similarly, a change in the technology may render the existing products obsolete, e.g., the colour television has made the black and white television out of fashion. Again a change in the fashion or customers’ taste may shift the demand in the market for a particular product, e.g., the demand for jeans reduced the sale of other traditional wear. All these aspects are external factors that are beyond the control of the business. So the business units must have to adapt themselves to these changes in order to survive and succeed in business.

INTERNATIONAL BUSINESS ENVIRONMENT

As firms expand to international markets, structural and environmental complexity and uncertainty increases, requiring managers to focus on the impact of the international business environment on their firms’ operations. International business environment is different from domestic business environment because the environment changes when a firm crosses international borders. Typically, a firm understands its domestic environment quite well, but is less familiar with the environment in other countries and must invest more time and resources into understanding the new environment.

Companies operating in international markets function in a highly competitive environment and require strategies that differentiate their products and enhance their perceived value, while reducing production costs. Companies operating internationally are affected by multiple environmental factors. They need to offer their product at competitive prices, and at the same time, tailor it to suit local needs. To bring down prices, they may be forced to

standardize the product and operate from a single location. However, customization of products to suit local preferences does not allow for standardization or location of the manufacturing unit in just one region. Customization rises a firm's operating costs. To cater to specific and special needs of local customers, the firm may have to set up similar facilities in several countries and modify their product features. Pressures from local competition for customization and price competition from international competitors with low-cost production bases pose a challenge to international companies. These companies have to choose between standardizing products, manufacturing at a low-cost location and passing the cost advantage to customers, and setting up plants in different countries for customizing products, regardless of the high costs that may be involved. Such companies have to frame a strategy that strikes a balance between these conflicting demands. For example, when a firm chooses a location for production, they have to consider various aspects like labour costs, tax rates, infrastructure, distribution systems, patent laws, suppliers and government support.

The IBE is multidimensional encompassing political risks, cultural differences, exchange risks, legal and taxation issues. Therefore IBE includes the political, economic, regulatory, tax, social and cultural, legal, and technological environments.

Political Environment:

The political environment refers to the type of government, the government relationship with business, and the political risk in a country. Doing business internationally thus implies dealing with different types of governments, relationships, and levels of risk.

The political environment in a country influences the legislations and government rules and regulations under which a foreign firm operates. Every country in the world follows its own system of law. A foreign company operating in that particular country has to abide with its system of law as long as it is operating in that country. Countries can be classified as free-market, centrally planned, or mixed. Free-market economies are those where government intervenes minimally in business activities, and market forces of supply and demand are allowed to determine production and prices. Centrally planned economies are those where the government determines production and prices based on forecasts of demand and desired levels of supply. Mixed economies are those where some activities are left to market forces and some, for national and individual welfare reasons, are government controlled. In the late twentieth century there has been a substantial move to free-market economies, but the People's Republic of China, the world's most populous country, along with a few others, remained largely centrally planned economies, and most countries maintain some government control of business activities.

There are many different types of political systems, for example, multi-party democracies, one-party states, constitutional monarchies, dictatorships (military and non-military). Also, governments change in different ways, for example, by regular elections, occasional elections, death, coups, war. Government-business relationships also differ from country to country. Business may be viewed positively as the engine of growth, it may be viewed negatively as the exploiter of the workers, or somewhere in between as providing both benefits and drawbacks. Specific government-business relationships can also vary from positive to negative depending on the type of business operations involved and the relationship between the people of the host country and the people of the home country. To be effective in a foreign location an international firm relies on the goodwill of the foreign government and needs to have a good understanding of all of these aspects of the political environment.

A particular concern of international firms is the degree of political risk in a foreign location. Political risk refers to the likelihood of government activity that has unwanted consequences for the firm. These consequences can be dramatic as in forced divestment, where a government requires the firm to give up its assets, or more moderate, as in unwelcome regulations or interference in operations. In any case the risk occurs because of uncertainty about the likelihood of government activity occurring. Generally, risk is associated with instability and a country is thus seen as more risky if the government is likely to change unexpectedly, if there is social unrest, if there are riots, revolutions, war, terrorism, and so on. Firms naturally prefer countries that are stable and that present little

political risk, but the returns need to be weighed against the risks, and firms often do business in countries where the risk is relatively high. In these situations, firms seek to manage the perceived risk through insurance, ownership and management choices, supply and market control, financing arrangements, and so on. In addition, the degree of political risk is not solely a function of the country, but depends on the company and its activities as well – a risky country for one company may be relatively safe for another. Thus, in analyzing political-legal environment, an organisation may broadly consider the following aspects:

- Political system of the business;
- Approaches of the Government towards business i.e., restrictive or facilitating;
- Facilities and incentives offered by the Government;
- Legal restrictions such as licensing requirement, reservation to a specific sector like public sector, private or small-scale sector;
- Restrictions in importing technical know-how, capital goods and raw materials;
- Restrictions in exporting products and services;
- Restrictions on pricing and distribution of goods;
- Procedural formalities required in setting the business.

Economic Environment

The economic environment relates to all the factors that contribute to a country's attractiveness for foreign businesses. The economic environment can be very different from one nation to another. Countries are often divided into three main categories: the more developed or industrialized, the less developed or third world, and the newly industrializing or emerging economies. Within each category there are major variations, but overall the more developed countries are the rich countries, the less developed the poor ones, and the newly industrializing (those moving from poorer to richer). These distinctions are usually made on the basis of gross domestic product per capita (GDP/capita). Better education, infrastructure, technology, health care, and so on are also often associated with higher levels of economic development. Clearly the level of economic activity combined with education, infrastructure, and so on, as well as the degree of government control of the economy, affect virtually all facets of doing business, and a firm needs to understand this environment if it is to operate successfully internationally. While analyzing the economic environment, the organisation intending to enter a particular business sector may consider the following aspects:

- Economic system to enter the business sector.
- Stage of economic growth and the pace of growth.
- Level of national and per capita income.
- Incidents of taxes, both direct and indirect.
- Infrastructure facilities available and the difficulties thereof.
- Availability of raw materials and components and the cost thereof.
- Sources of financial resources and their costs.
- Availability of manpower-managerial, technical and workers available and their salary and wage structures.

Technological Environment

The technological environment comprises factors related to the materials and machines used in manufacturing

goods and services. Receptivity of organisations to new technology and adoption of new technology by consumers influence decisions made in an organisation. As firms have no control over the external environment, their success depends upon how well they adapt to the external environment.

An important aspect of the international business environment is the level, and acceptance, of technological innovation in different countries. The last decades of the twentieth century saw major advances in technology, and this is continuing in the twenty-first century. Technology often is seen as giving firms a competitive advantage; hence, firms compete for access to the newest in technology, and international firms transfer technology to be globally competitive. It is easier than ever for even small businesses to have a global presence thanks to the internet, which greatly expands their exposure, their market, and their potential customer base. For economic, political, and cultural reasons, some countries are more accepting of technological innovations, others less accepting. In analyzing the technological environment, the organisation may consider the following aspects:

- Level of technological development in the country as a whole and specific business sectors.
- Pace of technological changes and technological obsolescence.
- Sources of technology.
- Restrictions and facilities for technology transfer and time taken for absorption of technology.

Cultural Environment

The cultural environment is one of the critical components of the international business environment and one of the most difficult to understand. This is because the cultural environment is essentially unseen; it has been described as a shared, commonly held body of general beliefs and values that determine what is right for one group, according to Kluckhohn and Strodtbeck. National culture is described as the body of general beliefs and values that are shared by a nation. Beliefs and values are generally seen as formed by factors such as history, language, religion, geographic location, government, and education; thus firms begin a cultural analysis by seeking to understand these factors. Firms want to understand what beliefs and values they may find in countries where they do business, and a number of models of cultural values have been proposed by scholars.

The most well-known is that developed by Hofstede in1980. This model proposes four dimensions of cultural values including individualism, uncertainty avoidance, power distance and masculinity.

- Individualism is the degree to which a nation values and encourages individual action and decision making.
- Uncertainty avoidance is the degree to which a nation is willing to accept and deal with uncertainty.
- Power distance is the degree to which a national accepts and sanctions differences in power.
- Masculinity is the degree to which a nation accepts traditional male values or traditional female values.

This model of cultural values has been used extensively because it provides data for a wide array of countries. Many academics and managers found this model helpful in exploring management approaches that would be appropriate in different cultures. For example, in a nation that is high on individualism one expects individual goals, individual tasks, and individual reward systems to be effective, whereas the reverse would be the case in a nation that is low on individualism.

While analyzing social and cultural factors, the organisation may consider the following aspects:

- Approaches of the society towards business in general and in specific areas;
- Influence of social, cultural and religious factors on acceptability of the product;
- Life style of people and the products useful for them;
- Level of acceptance of, or resistance to change;

- Values attached to a particular product i.e. possessive value or functional value in the product;
- Demand of specific products for specific occasions;
- Propensity to consume and to save.

Competitive Environment

The competitive environment also changes from country to country. This is partly because of the economic, political, and cultural environments; these environmental factors help determine the type and degree of competition that exists in a given country. Competition can come from a variety of sources. It can be public or private sector, come from large or small organizations, be domestic or global, and stem from traditional or new competitors. For the domestic firm the most likely sources of competition may be well understood. The same is not the case when one moves to compete in a new environment.

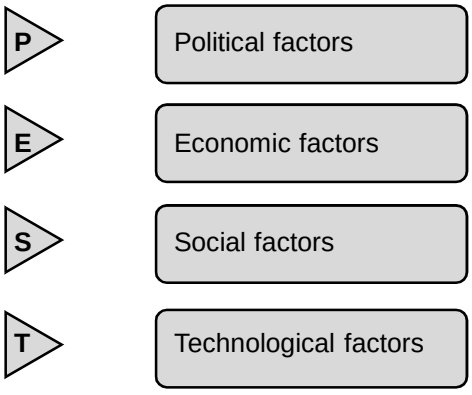
For example, in the 1990s in the United States most business was privately owned and competition was among private sector companies, while in the People's Republic of China (PRC) businesses were owned by the state. Thus, a U.S. company in the PRC could find itself competing with organizations owned by state entities such as the PRC army. This could change the nature of competition dramatically.

The nature of competition can also change from place to place like competition may be encouraged and accepted or discouraged in favour of cooperation; relations between buyers and sellers may be friendly or hostile; barriers to entry and exit may be low or high; regulations may permit or prohibit certain activities etc. To be effective internationally, firms need to understand these competitive issues and assess their impact.

TOOLS FOR INTERNATIONAL BUSINESS ENVIRONMENT ANALYSIS

1. PEST ANALYSIS

PEST analysis is an analysis of the political, economic, social and technological factors in the external environment of an organisation, which can affect its activities and performance. PEST analysis (Political, Economic, Social and Technological analysis) describes a framework of macro-environmental factors used in the environmental scanning component of international business management. It is a part of the external environmental analysis, and gives an overview of the different macro environmental factors that the company has to take into consideration. It is a useful strategic tool for understanding market growth or decline, business position, potential and direction for operations.



1. ***Political factors*** are basically to what degree the government intervenes in the economy. Specifically, political factors include areas such as tax policy, labour law, environmental law, trade restrictions, tariffs, and political stability. Political factors may also include goods and services which the government wants to provide or be provided (merit goods) and those that the government does not want to be provided

(demerit goods or merit bads). Furthermore, governments have great influence on the health, education, and infrastructure of a nation.

2. ***Economic factors*** include economic growth, interest rates, exchange rates and the inflation rate. These factors have major impacts on how businesses operate and make decisions. For example, interest rates affect a firm's cost of capital and therefore to what extent a business grows and expands. Exchange rates affect the costs of exporting goods and the supply and price of imported goods in an economy.
3. ***Social factors*** include the cultural aspects and include health consciousness, population growth rate, age distribution, career attitudes and emphasis on safety. Trends in social factors affect the demand for a company's products and how that company operates. For example, an aging population may imply a smaller and less-willing workforce (thus increasing the cost of labor). Furthermore, companies may change various management strategies to adapt to these social trends (such as recruiting older workers).
4. ***Technological factors*** include technological aspects such as R&D activity, automation, technology incentives and the rate of technological change. They can determine barriers to entry, minimum efficient production level and influence outsourcing decisions. Furthermore, technological shifts can affect costs, quality, and lead to innovation.

Harvard professor Francis Aguilar is thought to be the creator of PEST Analysis. He included a scanning tool called ETPS in his 1967 book "Scanning the Business Environment." The name was later tweaked to create the current acronym PEST.

Benefits

PEST Analysis is useful for four main reasons:

- It helps to spot business or personal opportunities, and it gives advanced warning of significant threats.
- It reveals the direction of change within the business environment. This helps to shape the business accordingly.
- It helps avoid starting the projects that are likely to fail, for reasons beyond the control of firms.
- It helps to develop an objective view of new environment while entering a new country, region, or market.

Gathering information is the a first important step in doing PEST analysis. Once it is done, the information has to be evaluated. There are many factors changing in the external environment but not all of them are affecting or might affect the organisation. Therefore, it is essential to identify which PEST factors represent the opportunities or threats for an organisation and list only those factors in PEST analysis. This allows focusing on the most important changes that might have an impact on the company.

Political Factors to Consider

- When is the country's next local, state, or national election? How could this change government or regional policy?
- Who are the most likely contenders for power? What are their views on business policy, and on other policies that affect your organisation?
- Depending on the country, how well developed are property rights and the rule of law, and how widespread are corruption and organized crime? How are these situations likely to change, and how is this likely to affect you?
- Could any pending legislation or taxation changes affect your business, either positively or negatively?

- How will business regulation, along with any planned changes to it, affect your business? And is there a trend towards regulation or deregulation?
- How does government approach corporate policy, corporate social responsibility, environmental issues, and customer protection legislation? What impact does this have, and is it likely to change?
- What is the likely timescale of proposed legislative changes?
- Are there any other political factors that are likely to change?

Economic Factors to Consider

- How stable is the current economy? Is it growing, stagnating, or declining?
- Are key exchange rates stable, or do they tend to vary significantly?
- Are customers' levels of disposable income rising or falling? How is this likely to change in the next few years?
- What is the unemployment rate? Will it be easy to build a skilled workforce? Or will it be expensive to hire skilled labor?
- Do consumers and businesses have easy access to credit? If not, how will this affect your organisation?
- How is globalization affecting the economic environment?
- Are there any other economic factors that you should consider?

Socio-Cultural Factors to Consider

- What is the population's growth rate and age profile? How is this likely to change?
- Are generational shifts in attitude likely to affect what you're doing?
- What are your society's levels of health, education, and social mobility? How are these changing, and what impact does this have?
- What employment patterns, job market trends, and attitudes toward work can you observe? Are these different for different age groups?
- What social attitudes and social taboos could affect your business? Have there been recent socio-cultural changes that might affect this?
- How do religious beliefs and lifestyle choices affect the population?
- Are any other socio-cultural factors likely to drive change for your business?

Technological Factors to Consider

- Are there any new technologies that you could be using?
- Are there any new technologies on the horizon that could radically affect your work or your industry?
- Do any of your competitors have access to new technologies that could redefine their products?
- In which areas do governments and educational institutions focus their research? Is there anything you can do to take advantage of this?
- How have infrastructure changes affected work patterns (for example, levels of remote working)?
- Are there existing technological hubs that you could work with or learn from?
- Are there any other technological factors that you should consider?

The factors given above will vary in importance to a given company based on its industry and the goods it produces. For example, consumer and B2B companies tend to be more affected by the social factors, while a global defense contractor would tend to be more affected by political factors. Additionally, factors that are more likely to change in the future or more relevant to a given company will carry greater importance. For example, a company which has borrowed heavily will need to focus more on the economic factors (especially interest rates).

Furthermore, conglomerate companies who produce a wide range of products (such as Sony or Disney) may find it more useful to analyze one department of its company at a time focusing on the specific factors relevant to that one department.

PEST analysis template

PEST analysis template	
Political	**Economic**
– Government stability and likely changes	– Growth rates
– Bureaucracy	– Inflation rate
– Corruption level	– Interest rates
– Tax policy (rates and incentives)	– Exchange rates
– Freedom of press	– Unemployment trends
– Regulation/de-regulation	– Labor costs
– Trade control	– Stage of business cycle
– Import restrictions (quality and quantity)	– Credit availability
– Tariffs	– Trade flows and patterns
– Competition regulation	– Level of consumers' disposable income
– Government involvement in trade unions and agreements	– Monetary policies
– Environmental Law	– Fiscal policies
– Education Law	– Price fluctuations
– Anti-trust law	– Stock market trends
– Discrimination law	– Weather
– Copyright, patents / Intellectual property law	– Climate change
– Consumer protection and e-commerce	
– Employment law	
– Health and safety law	
– Data protection law	
– Laws regulating environment pollution	

Socio-cultural	Technological
– Health consciousness	– Basic infrastructure level
– Education level	– Rate of technological change
– Attitudes toward imported goods and services	– Spending on research & development
– Attitudes toward work, leisure, career and retirement	– Technology incentives
– Attitudes toward product quality and customer service	– Legislation regarding technology
– Attitudes toward saving and investing	– Technology level in your industry
– Emphasis on safety	– Communication infrastructure
– Lifestyles	– Access to newest technology
– Buying habits	– Internet infrastructure and penetration
– Religion and beliefs	
– Attitudes toward “green” or ecological products	
– Attitudes toward and support for renewable energy	
– Population growth rate	
– Immigration and emigration rates	
– Age distribution and life expectancy rates	
– Sex distribution	
– Average disposable income level	
– Social classes	
– Family size and structure	
– Minorities	

PEST and SWOT

The PEST factors, combined with external micro-environmental factors and internal drivers, can be classified as opportunities and threats in a SWOT analysis. PEST Analysis is often linked with SWOT Analysis, however, the two tools have different areas of focus. PEST Analysis looks at “big picture” factors that might influence a decision, a market, or a potential new business. SWOT Analysis explores these factors at a business, product-line or product level. These tools complement one another and are often used together.

PEST analysis is also done to assess the potential of a new market. The general rule is that the more negative forces are affecting that market the harder it is to do business in it. The difficulties that will have to be dealt with significantly reduce profit potential and the firm can simply decide not to engage in any activity in that market.

PEST variations

PEST analysis is the most general version of all PEST variations created. It is a very dynamic tool as new components can be easily added to it in order to focus on one or another critical force affecting the company. Although following variations are more detailed analysis than simple PEST, the additional components are just the extensions of the same PEST factors. These include:

STEP = PEST in more positive approach.

PESTEL = PEST + Environmental + Legal

PESTELI = PESTEL + Industry analysis

STEEP = PEST + Ethical

SLEPT = PEST + Legal

STEEPLE = PEST + Environmental + Legal + Ethical

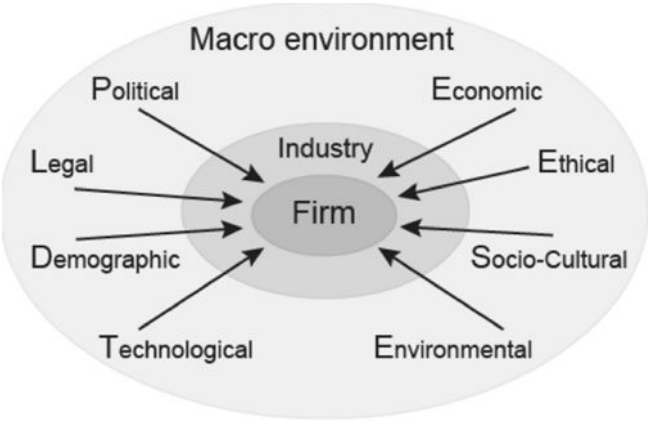
STEEPLED = STEEPLE + Demographic

PESTLIED = PEST + Legal + International + Environmental + Demographic

LONGPEST = Local + National + Global factors + PEST

2. PESTEL MODEL

It involves the collection and portrayal of information about internal and external factors which have, or may have, an impact on business. PESTEL analysis is a simple and effective tool used in situation analysis to identify the key external (the macro environment level) forces that might affect an organisation. These forces can create both opportunities and threats for an organisation. PESTEL model is PEST including legal, environmental, ethical and demographic forces.



Pestel Analysis Template	
Political (from PEST analysis)	**Economic (from PEST analysis)**
Socio-cultural (from PEST analysis)	**Technological (from PEST analysis)**
Environmental (ecological)	**Legal**
– Weather – Climate change – Laws regulating environment pollution – Air and water pollution – Recycling – Waste management – Attitudes toward “green” or ecological products	– Anti-trust law – Discrimination law – Copyright, patents / Intellectual property law – Consumer protection and e-commerce – Employment law – Health and safety law – Data Protection

– Endangered species – Attitudes toward and support for renewable energy	

STEEPLED analysis template	
Political (from PEST analysis)	**Economic** (from PEST analysis)
Socio-cultural (from PEST analysis)	**Technological** (from PEST analysis)
Environmental (ecological) (from PESTEL analysis)	**Legal** (from PESTEL analysis)
Ethical	**Demographic**
– Ethical advertising and sales practices – Accepted accounting, management and marketing standards – Attitude towards counterfeiting and breaking patents – Ethical recruiting practices and employment standards (not using children to produce goods)	– Population growth rate – Immigration and emigration rates – Age distribution and life expectancy rates – Sex distribution – Average disposable income level – Social classes – Family size and structure – Minorities

CASE STUDY - PREMIER INN'S PESTLE ANALYSIS

The Whitbread PLC story began in 1742 when Samuel Whitbread opened his first brewery. In 1750, Whitbread PLC moved to premises in Chiswell Street, London and was the first purpose-built mass-production brewery in Britain. Whitbread PLC became a well-known brand name in the brewery industry until 2001 when Whitbread PLC sold its breweries and left the pubs and bars business. Whitbread PLC had diversified in a variety of different industries including wines, spirits and nightclubs but decided to refocus its business on its leading growth areas, hotels and restaurants.

Premier Inn is one of the major brands of Whitbread PLC (Other Brands Include: Costa Coffee, Taybarns, Brewers Fayre, Table Table and Beefeater Grill). Premier Inn is the UK's largest hotel brand with occupancy rates of over 80% in more than 590 budget hotels with over 43,000. Premier Inns' location is paramount to its success as most are found along major roads and in regional towns and cities. Premier Inns' brand promise is to give you 'a good sleep, night after night after night – consistently do the extra-ordinary'.

Premier Inn is an award winning hotel chain and has geographical spread to facilitate 75% of the UK population in a radius of five miles. Premier Inn's bedrooms all have an attached bathroom, TV with Free view, and Wi-Fi internet access. All hotels comprises of a bar and restaurant, either inside the building, or next to it, offering and serving a wide range of dishes. All these facilities and services are offered at a very cheap price starting from just £29 per night (terms and conditions apply).

They are also expanding their hotel chains internationally. In this regard Premier Inn has opened one hotel in Dubai and two in India. This is just the start of expanding geographical spread around the world.

Mission and Vision

"We want to make our hospitality brands the best they can be by focussing on our customers and giving them just what they want"

Premier Inn Standards

- Offer 100% money back guarantee of quality room to customers
- Comfortable surrounding
- Friendly servic

They call it "Good Night Guarantee"

Future Plans

- Big expansion plan of adding another 55,000 rooms by 2014 to cement the current position as the UK's biggest hotel chain
- Aiming and planning to be the biggest budget hotel chain in London by 2012
- Planning to open more hotels in overseas

Management Board

- Premier Inn brand is management by an independent Management Board which consists of highly professional executives teams.

Customers Insight

In 2009-10 Premier Inn initiated a program to understand the customer more effectively and vigilantly. They have evolved their strategy on customer feedback. The deep insight in customer's feedback provides them to initiate their programs more efficiently which leads them to winning and retaining customers. They hold regular Focus Group meeting to explore thought and feelings of customers. Their customer feedback program mainly includes:

- Premier Inn Guest Satisfaction Survey: The biggest in Europe
- Premier Offers with rooms from £29: Inspired by our customers
- Brand standards: Maintain consistency across our Hotels and Restaurants
- Using YouGov Brand Index to compare performance with other leading brands

Corporate Responsibility

Premier Inn is committed to Corporate Responsibility Programs "Good Together". They are continuously building their values. They have long history of community development programs. The corporate responsibility is an integral part of their businesses. The corporate responsibility of Premier Inn is focused on six priority areas (i.e. Environment, People, Sourcing, Health, Community and Customers). They keep devising a more committed strategy across these areas.

From the information given above and using sources from internet, conduct PESTEL Analysis of the Premier Inn.

Hints:

PESTEL Analysis	
Political	**Economic**
■ Positive and pragmatic collaboration with UK Government has brought Hospitality Industry into key success area of economic development in UK.	■ The budget hotel sector has been one of the greatest success stories in the UK hospitality industry over the last 10-15 years, and continues to be so.
■ Hospitality is the UK's fifth largest industry, directly employing more than 2.4 m people and contributing over £34bn in gross tax revenues.	■ It is estimated that UK budget hotel sector is going to be more than double in size in next 20 years and will account for more than a quarter of the overall hotel market by 2027.
■ As the generator of eight per cent of total employment, the industry is ahead of the financial services, transport and communications, and constructions sectors.	■ The UK budget hotel market has also broken the £1b barrier for the first time in 2006, new research has revealed.
■ Prime Minister David Cameron has recognised that tourism is one of five 'big-ticket' industries of the future and one that the government 'should get behind' especially as for every 0.5% increase in the UK's share of the global tourism can add £2.7b to the economy and create 50,000 jobs.	■ The current growth in supply and market volume has increased considerably as leading operators are engaged in a frantic scramble for market dominance. World over tourism and hospitality sector is generating more and more profits.
■ Establishment of regional growth fund for hospitality industry is also a major sign of expected growth in the sector. Hospitality could generate 236,000 net additional jobs across the UK by 2015 bringing the total number employed by the British Hospitality Industry to 2.76 million.	■ This is a very encouraging factor for Premier Inn for expansion of their budget hotel chains. Currently Premier Inn is the UK's largest and fastest-growing budget hotel chain, with over 590 budget hotels and more than 43,000 rooms across the UK and Ireland. They have big expansion plans and aim to add another 55,000 rooms by 2014.
Socio-cultural	**Technological**
■ The social circles and changing life styles & living standards has brought many social and cultural changes around the world. As the living costs are increasing, people prefer low cost products/ services accompanied with highest standard of value for money.	■ The operations of hospitability does not involves high level of technology and the focus of technology is budget hotel sector is directly linked with availability of electrical appliances and availability of IT services for comfort of customers.
■ These social changes are bringing different thought patterns. These social changes also influencing the hospitality sector around the world.	■ The use of latest development in IT helps in maintain smooth functioning for hotel chains across the region. It also helps them to develop centralized supply chain management systems.
■ Premier Inn is focused on customer satisfactions and keeping revitalizing there business strategy with changing social values and customer preferences.	■ Technology is largely influencing the marketing and promotion of the products. The way of communication is changing to web based techniques. Premier Inn is also maintaining a good

■ They offer to their customers a 100% money-back guarantee of a good quality room, comfortable surroundings and friendly service (Whitbread Co). ■ They are committed to understand their customers better than anyone else.	look and interactive website in this regard. ■ The online reservation facilitation services are available. They also maintain a database of customers and keep sending messages regarding new product offering and promotional campaign. Use of mobile is also providing a big platform for advertisement and awareness campaign.
Environmental (ecological)	**Legal**
■ The strong emphasis on Corporate Social Responsibility (CRS) is one of the major core competencies of Premier Inn. ■ They have developed a strong CRS Strategy for "Good Together" and Whitbread way forward. ■ In 2008 they have reviewed their corporate responsibility strategy and created "Good Together" programme. ■ Premier Inn's approach to the environment is guided by their environment policy and energy policy, which contain a number of principles which they are required to comply.	■ The minimum wage rate has been increased 15.5% by UK Government that would costs an increase in operating cost of budget hotels. ■ This would increase cost of production which hampers the policy to offer competitive prices to customers. ■ To avoid legal issues and maintain high standard they have developed a Responsible Sourcing Policy, which defines the minimum standards and principles of cooperation that Premier Inn expect from suppliers, contractors and business partners.

3. SWOT ANALYSIS

It is an analysis of an organisation's strengths and weaknesses alongside the opportunities and threats present in the external environment. It involves the collection and portrayal of information about internal and external factors which have, or may have, an impact on business. It is a framework that allows managers to synthesize insights obtained from an internal analysis of the company's strengths and weaknesses with those from an analysis of external opportunities and threats. SWOT is an acronym which stands for:

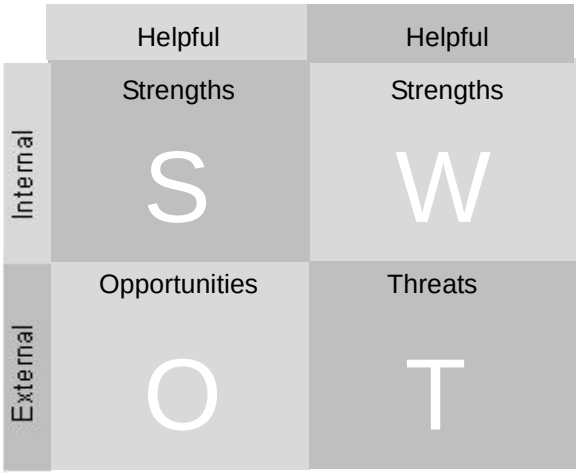
1. Strengths: factors that give an edge for the company over its competitors.

2. Weaknesses: factors that can be harmful if used against the firm by its competitors.

3. Opportunities: favorable situations which can bring a competitive advantage.

4. Threats: unfavorable situations which can negatively affect the business.

Strengths and weaknesses are internal to the company and can be directly managed by it, while the opportunities and threats are external and the company can only anticipate and react to them. Often, swot is presented in a form of a matrix as in the illustration below:



Swot is widely accepted tool due to its simplicity and value of focusing on the key issues which affect the firm. The aim of swot is to identify the strengths and weaknesses that are relevant in meeting opportunities and threats in particular situation.

Benefits: Swot tool has 5 key benefits:

- Simple to do and practical to use;
- Clear to understand;
- Focuses on the key internal and external factors affecting the company;
- Helps to identify future goals;
- Initiates further analysis.

Limitations

Although there are clear benefits of doing the analysis, many managers and academics heavily criticize or don't even recognize it as a serious tool. According to many it is a 'low-grade' analysis. Here are the main flaws identified by the research:

- Excessive lists of strengths, weaknesses, opportunities and threats;
- No prioritization of factors;
- Factors are described too broadly;
- Factors are often opinions not facts;
- No recognized method to distinguish between strengths and weaknesses, opportunities and threats.

Performing the analysis?

Swot can be done by one person or a group of members that are directly responsible for the situation assessment in the company. Basic swot analysis is done fairly easily and comprises of only few steps:

Step 1: Listing the firm's key strengths and weaknesses

- Strengths and weaknesses are the factors of the firm's internal environment.
- When looking for strengths, ask "what do you do better or have more valuable than your competitors have?"

- In case of the weaknesses, ask "what could you improve and at least catch up with your competitors?"
- Strengths and weaknesses can be identified from the firm's
  - Resources: land, equipment, knowledge, brand equity, intellectual property, etc.
  - Core competencies
  - Capabilities
  - Functional areas: management, operations, marketing, finances, human resources and R&D
  - Organisational culture
  - Value chain activities
- Any internal factor can be either strength or weakness. The manager will have to analyse it depending upon the available information and circumstances. A resource can be seen as a strength if it exhibits VRIO (valuable, rare and cannot be imitated) framework characteristics. Otherwise, it doesn't provide any strategic advantage for the company For example:
  - "Brand image" might be a weakness if the company has poor brand image. However, it can also be strength if the company has the most valuable brand in the market.
  - 17% profit margin would be an excellent margin for many firms in most industries and it would be considered as strength. But what if the average profit margin of your competitors is 20%? Then company's 17% profit margin would be considered as a weakness.

Step 2: Identifying opportunities and threats

- Opportunities and threats are the external uncontrollable factors.
- They arise due to the changes in the macro environment, industry or competitors' actions.
- Opportunities represent the external situations that bring a competitive advantage if seized upon.
- Threats damage your company so you would better avoid or defend against them.
- Any external factor can be either strength or weakness. The manager will have to analyse it depending upon the available information and circumstances. The organisation can only guess the outcome and count on analysts' forecasts. For example, exchange rates may increase or reduce the profits from exports, depending if the exchange rate of currency will rise (opportunity) or fall (threat) against the other currencies.

Guidelines for successful SWOT

The following guidelines are very important in writing a successful swot analysis. They eliminate most of swot limitations and improve it significantly:

- Factors have to be identified relative to the competitors. It allows specifying whether the factor is a strength or a weakness.
- List between 5 – 10 items for each category. Prevent creating too short or endless lists.
- Items must be clearly defined and as specific as possible. For example, firm's strength is: brand image (vague); strong brand image (more precise); brand image valued at $10 billion, which is the most valued brand in the market (very good).
- Rely on facts not opinions. Find some external information or involve someone who could provide an unbiased opinion.

– Factors should be action orientated. For example, “slow introduction of new products” is action orientated weakness.

SWOT analysis template

SWOT analysis of Company “A”

	Strengths		**Weaknesses**
1.	Second most valuable brand in the world valued at $76 billion	1.	Investments in R&D are below the industry average
2.	Diversified income (5 different brands earning more than $4 billion each)	2.	Very low or zero profit margins
3.	Strong patents portfolio (15,000 patents)	3.	Poor customer services
4.	Investments in R&D reaching 4 billion a year.	4.	High employee turnover
5.	Competent in mergers & acquisitions	5.	High cost structure
6.	Have an access to cheap cash reserves	6.	Weak brand portfolio
7.	Effective corporate social responsibility (CSR) projects	7.	Rigid (bureaucratic) organisational culture impeding fast introduction of new products
8.	Localized products	8.	High debt level ($3 billion)
9.	Highly skilled workforce	9.	Brand dilution (the firm has too many brands)
10.	Economies of scale or economies of scope	10.	Poor presence in the world’s largest markets
	Opportunities		**Threats**
1.	Market growth for the main firm’s product	1.	Corporate tax may increase from 20% to 22% in the financial year
2.	Growing demand for renewable energy	2.	Rising pay levels
3.	New technology, that would drive production costs by 20% is in development	3.	Rising raw material prices
4.	Our country accession to EU	4.	Intense competition
5.	Changing customer habits	5.	Market is expected to grow by only 1% next year indicating market saturation
6.	Disposable income level will increase	6.	Increasing fuel prices
7.	Government’s incentives for ‘specific’ industry	7.	Aging population
8.	Economy is expected to grow by 4% next year	8.	Stricter laws regulating environment pollution
9.	Growing number of people buying online	9.	Lawsuits against the company
10.	Interest rates falling to 1%	10.	Currency fluctuations

Case study: SWOT analysis of Ford MOTOR Company



Ford Motor Company is one of the first American automotive companies that even today successfully manufactures and sells automobiles, trucks, buses and automotive parts. Ford is the second largest US automaker and the fifth largest vehicle seller in Europe and the world.

Henry Ford began his unprecedented foray into the automobile industry in 1899 with the founding of the Detroit Automobile Company. Four years later, through a set of trials and tribulations, Ford Motor Company was incorporated with 12 investors holding 1000 shares The Ford Model T built in 1908, was the automobile that shared the spotlight during the creation of the first assembly line in 1913. Henry Ford had his eyes wide open to various business expansion possibilities early, establishing Ford of Canada in 1904 and jumping into European markets by 1911. Though Ford Motor Company has had its pitfalls, i.e. the Edsel model, they have continued to be a driving force in the automobile industry. Most recently, Ford Motor Company was the only one of the top three automobile makers in the United States not to take bailout money. Instead, Ford mortgaged all of its assets to raise the $23.4 billion dollars within its own corporation.

Ford had an outstanding year in 2013, the fourth in a row. The Company's pre-tax operating profit was among the best in our history and automotive operating-related cash flow was a record since at least 2001. These full-year results reflect an automotive sector operating profit that was the highest in more than a decade with record profits in North America and Asia Pacific Africa, about break-even result in South America, and a lower loss in Europe than last year.

Ford Credit was solidly profitable. Volume and revenue grew compared to last year with market share gains in the United States, South America, and in Asia Pacific Africa, which was driven by record market share in China. Retail share was also higher in Europe.

Consistent with plan to provide regular growing dividends that are sustainable over an economic or business cycle, the dividend doubled in 2013 and announced an additional 25% increase for the first quarter of 2014. In addition, four of the major rating agencies that rate us now report Ford and Ford Credit as investment grade. The Company has made tremendous progress in recent years.

Read full annual report of the Ford Motor Company from its website and perform the SWOT analysis.

Hints:

Strengths	**Weaknesses**
1. Strong position in US market 2. ECOnetic initiative 3. Sound financial performance 4. 'One Ford' approach 5. Significant growth in China	1. Poor environmental record 2. High cost structure 3. Unprofitable Europe operations
Opportunities	**Threats**
1. Positive attitude towards "green" vehicles 2. Increasing fuel prices 3. New emission standards	1. Decreasing fuel prices 2. Rising raw material prices 3. Intense competition

4. Growth through acquisitions	4. Fluctuating exchange rates

Strengths

1. **Strong position in US market.** Ford is the second largest automaker in US, the second largest vehicle market in the world. Ford has great reputation in its home market and strong commercial vehicle sales that are the most profitable Ford's vehicles.
2. **ECOnetic initiative.** Ford's ECOnetic initiative is an effort to produce highly fuel-efficient engines by improving existing engines rather than new hybrid engines. The result of this initiative is the Ford Fiesta, currently the lowest emitting mass-produced car in Europe and Ford Focus ECOnetic that has better fuel consumption that Toyota Prius.
3. **Sound financial performance.** Ford was the only big US car company that didn't need the government bailout and was the first to get investment status back. The firm's profit margin is high compared to competitors with the highest liquidity ratio.
4. **'One Ford' approach.** Ford has decided to produce single, streamlined global lineup of its models. The carmaker no longer produces customized vehicles for different regions but focus on designing and engineering the car that fits different regional tastes and regulations. It significantly decreases costs for Ford and drives record profitability.
5. **Significant growth in China.** Ford, although not the strongest player in the China has experienced the significant growth in the largest automotive market in the world for the 2012. It grew its sales by 46%, according to Ford press release.

Weaknesses

1. **Poor environmental record.** Ford has been criticized for poor efforts to decrease environment pollution. University of Massachusetts Amherst have rated Ford as the seventh worst air polluter due to its manufacturing plants. The US Environmental Protection Agency also linked Ford to 42 toxic waste sites.
2. **High cost structure.** Although 'One Ford' initiative led to substantial cost reduction, Ford still has a high cost structure, compared to other automobiles manufacturers. Ford's costs are driven by its generous employee compensation and pension plans.
3. **Unprofitable Europe operations.** In 2012, Ford lost $1.75 billion in Europe and plans to experience losses in the region until 2015.

Opportunities

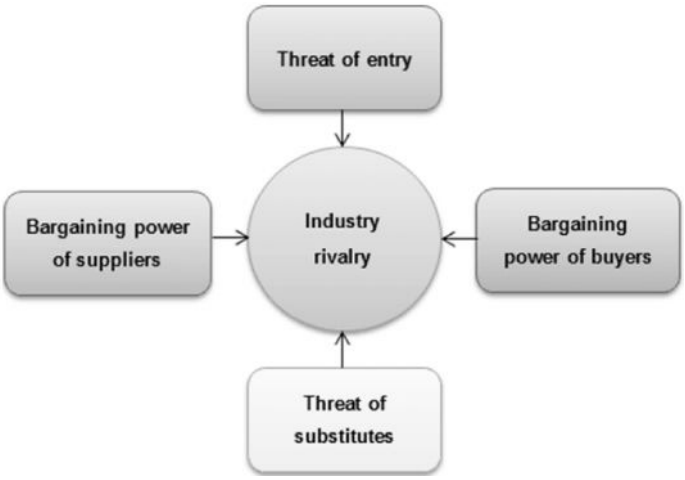
1. **Positive attitude towards "green" vehicles.** Cars that are fuel inefficient and emit large quantities of CO2 heavily pollute air and negatively affect the environment. Consumers are aware of this negative impact and are more likely to buy "green" vehicles that emit much less CO2 and are fuel-efficient.
2. **Increasing fuel prices.** Ford's strong emphasis on engineering fuel-efficient vehicles (Ford Fiesta and Ford Focus ECOnetic) with flexible fuel and hybrid engines will pay off due to increasing fuel prices in the world.
3. **New emission standards.** A new wave for stricter regulations on vehicle emission standards would positively affect Ford position in automotive industry. Ford invests large amounts of money to produce fuel-efficient engines and reaped some success with its ford Fiesta and Ford Focus ECOnetic models.
4. **Strategic partnerships.** Ford has great experience in creating strategic alliances and partnerships with other automotive companies. Due to current competitive pressure, all companies are more likely to enter into such partnerships to drive R&D costs down, access new markets and gain some new skills.

Threats

1. **Decreasing fuel prices.** Some analysts forecast that future fuel prices will drop due to extraction of shale gas. This would negatively affect Ford as it focus on compact fuel-efficient hybrid and flexible fuel cars that are less attractive when the fuel price is low.
2. **Rising raw material prices.** Rising prices for raw metals will lift the costs for auto manufacturers and result in squeezed profits for the companies.
3. **Intense competition.** Ford faces more intense competition from other auto manufacturers more than ever, especially in small cars segment with hybrid engines.
4. **Fluctuating exchange rates.** Ford, including other largest automotive companies, may negatively be affected by fluctuating exchange rates as it earns more than half of its profits outside the US. The profits may be lower due appreciating dollar against other currencies.

4. PORTER'S FIVE FORCES MODEL

Porter's five forces model is an analysis tool that uses five forces to determine the profitability of an industry and shape a firm's competitive strategy. It is a framework that classifies and analyzes the most important forces affecting the intensity of competition in an industry and its profitability level. Five forces model was created by Michael Porter in 1979 to understand how five key competitive forces are affecting an industry. The five forces identified are:



These forces determine an industry structure and the level of competition in that industry. An industry with low barriers to enter, having few buyers and suppliers but many substitute products and competitors will be seen as very competitive and thus, not so attractive due to its low profitability.



It is every strategist's job to evaluate company's competitive position in the industry and to identify what strengths or weakness can be exploited to strengthen that position. The tool is very useful in formulating firm's strategy as it reveals how powerful each of the five key forces is in a particular industry.

***Threat of new entrants*:** This force determines how easy (or not) it is to enter a particular industry. If an industry is profitable and there are few barriers to enter, rivalry soon intensifies. When more organisations compete for the same market share, profits start to fall. It is essential for existing organisations to create high barriers to enter to deter new entrants. Threat of new entrants is high when:

- Low amount of capital is required to enter a market;
- Existing companies can do little to retaliate;
- Existing firms do not possess patents, trademarks or do not have established brand reputation;
- There is no government regulation;
- Customer switching costs are low (it doesn't cost a lot of money for a firm to switch to other industries);
- There is low customer loyalty;
- Products are nearly identical;
- Economies of scale can be easily achieved.

***Bargaining power of suppliers*:** Strong bargaining power allows suppliers to sell higher priced or low quality raw materials to their buyers. This directly affects the buying firms' profits because it has to pay more for materials. Suppliers have strong bargaining power when:

- There are few suppliers but many buyers;
- Suppliers are large and threaten to forward integrate;
- Few substitute raw materials exist;
- Suppliers hold scarce resources;
- Cost of switching raw materials is especially high.

Bargaining power of buyers: Buyers have the power to demand lower price or higher product quality from industry producers when their bargaining power is strong. Lower price means lower revenues for the producer, while higher quality products usually raise production costs. Both scenarios result in lower profits for producers. Buyers exert strong bargaining power when:

- Buying in large quantities or control many access points to the final customer;
- Only few buyers exist;
- Switching costs to other supplier are low;
- They threaten to backward integrate;
- There are many substitutes;
- Buyers are price sensitive.

Threat of substitutes: This force is especially threatening when buyers can easily find substitute products with attractive prices or better quality and when buyers can switch from one product or service to another with little cost. For example, to switch from coffee to tea doesn't cost anything, unlike switching from car to bicycle.

***Rivalry among existing competitors*:** This force is the major determinant on how competitive and profitable an industry is. In competitive industry, firms have to compete aggressively for a market share, which results in low profits. Rivalry among competitors is intense when:

- There are many competitors;
- Exit barriers are high;
- Industry of growth is slow or negative;
- Products are not differentiated and can be easily substituted;
- Competitors are of equal size;
- Low customer loyalty.

Although, Porter originally introduced five forces affecting an industry, scholars have suggested including the sixth force: complements. Complements increase the demand of the primary product with which they are used, thus, increasing firm's and industry's profit potential. For example, iTunes was created to complement iPod and added value for both products. As a result, both iTunes and iPod sales increased, increasing Apple's profits.

Performing the Analysis

We now understand that Porter's five forces framework is used to analyze industry's competitive forces and to shape organisation's strategy according to the results of the analysis. But how to use this tool? We have identified the following steps:

- Step 1. Gather the information on each of the five forces
- Step 2. Analyze the results and display them on a diagram
- Step 3. Formulate strategies based on the conclusions

***Step 1*:** Gather the information on each of the five forces. What managers should do during this step is to gather information about their industry and to check it against each of the factors (such as "number of competitors in the industry") influencing the force. A template with the most important factors is given below.

Threat of new entry	**Supplier power**	**Buyer power**
– Amount of capital required	– Number of suppliers	– Number of buyers
– Retaliation by existing companies	– Suppliers' size	– Size of buyers
– Legal barriers (patents, copyrights, etc.)	– Ability to find substitute materials	– Size of each order
– Brand reputation	– Materials scarcity	– Buyers' cost of switching suppliers
– Product differentiation	– Cost of switching to alternative materials	– There are many substitutes
– Access to suppliers and distributors	– Threat of integrating forward	– Price sensitivity
– Economies of scale		– Threat of integrating backward
– Sunk costs		
– Government regulation		
Threat of substitutes	**Rivalry among existing competitors**	

– Number of substitutes – Performance of substitutes – Cost of changing	– Number of competitors – Cost of leaving an industry – Industry growth rate and size – Product differentiation – Competitors' size – Customer loyalty – Threat of horizontal integration – Level of advertising expense	

***Step 2*:** Analyze the results and display them on a diagram. After gathering all the information, analyze it and determine how each force is affecting an industry. For example, if there are many companies of equal size operating in the slow growth industry, it means that rivalry between existing companies is strong. Remember that five forces affect different industries differently so don't use the same results of analysis for even similar industries!

Step 3: Formulate strategies based on the conclusions. At this stage, managers should formulate firm's strategies using the results of the analysis For example, if it is hard to achieve economies of scale in the market, the company should pursue cost leadership strategy. Product development strategy should be used if the current market growth is slow and the market is saturated.

Porter's five forces is a great tool to analyze industry's structure and formulate firm's strategy, it can be done with SWOT, PEST or Value Chain analysis for further value additions.

CASE STUDY - PORTER'S FIVE FORCES ANALYSIS OF INDIAN AUTOMOBILE INDUSTRY

The automobile industry is one of India's most vibrant and growing industries. This industry accounts for 22 per cent of the country's manufacturing gross domestic product (GDP). The auto sector is one of the biggest job creators, both directly and indirectly. It is estimated that every job created in an auto company leads to three to five indirect ancillary jobs. India's domestic market and its growth potential have been a big attraction for many global automakers. India is presently the world's third largest exporter of two-wheelers after China and Japan. According to a report by Standard Chartered Bank, India is likely to overtake Thailand in global auto-export market share by the year 2020.

The next few years are projected to show solid but cautious growth due to improved affordability, rising incomes and untapped markets. With the government's backing, and trends in the international scenario such as the decline in prices of natural rubber, the Indian automobile industry is slated to witness some major growth.

Market size

The cumulative foreign direct investment (FDI) inflows into the Indian automobile industry during the period April 2000 – August 2014 was recorded at US$ 10,119.68 million, as per data by Department of Industrial Policy and Promotion (DIPP). Data from industry body Society of Indian Automobile Manufacturers (SIAM) showed that 137,873 passenger cars were sold in July 2014 compared to 131,257 units during the corresponding month of 2013. Among the auto makers, Maruti Suzuki, Hyundai Motor India and Honda Cars India emerged the top three gainers with sales growth of 15.45 per cent, 12 per cent and 11 per cent, respectively. The three-wheeler segment posted a 24 per cent growth to 51,461 units on the back of increased demands from the

urban market. Total sales across different vehicle segments grew 12 per cent year on year (y-o-y) to 1,586,123 units. Scooter sales have jumped by 29 per cent in the ongoing fiscal, and now form 27 per cent of the total two-wheeler market from just 8 per cent a decade back. The ever-rising demand for scooters, which has far outstripped supply has prompted Honda to set up its first dedicated scooter plant in Ahmedabad. Tractor sales in the country is expected to grow at a compound annual growth rate (CAGR) of 8–9 per cent in the next five years making India a high-potential market for many international brands.

Investments

To match production with demand, many auto makers have started to invest heavily in various segments in the industry in the last few months. Some of the major investments and developments in the automobile sector in India are as follows:

- Ashok Leyland plans to invest Rs 450–500 crore (US$ 73.54–81.71 million) in India, by way of capital expenditure (capex) and investment during FY15. The company is required to manage Rs 6,000 crore (US$ 980.56 million) of assets in seven locations across the world, for which maintenance capex is needed.
- Honda Motors plans to set up the world's largest scooter plant in Gujarat to roll out 1.2 million units annually and achieve leadership position in the Indian two-wheeler market. The company plans to spend around Rs 1,100 crore (US$ 179.76 million) on the new plant in Ahmedabad, and expand its range with a few more offerings.
- Yamaha Motor Co has restructured its business in India. Now, Yamaha Motor India (YMI) will take care of its India operations. "The restructuring is part of Yamaha's mid-term plan aimed at improving organisational efficiency," as per Mr Hiroyuki Suzuki, Chief Executive and Managing Director. YMI would be responsible for corporate planning and strategy, business planning and business expansion, quality control, and regional control of Yamaha India Business.
- Tata Motors plans to use the 'hub-and-spoke' model in which India will be the key manufacturing base while it will have mini-hubs in overseas markets. The company also plans to set up mini hubs in potential markets like Africa, Middle-East and South East Asia.
- Hero Cycles through its unit OPM Global has acquired a majority stake in German bicycle company Mitteldeutsche Fahrradwerke AG (MIFA) for €15 million (US$ 19.11 million). The company plans to invest an additional €4 million (US$ 5.09 million) as capital expenses in restructuring the acquired company.

Government Initiatives

The Government of India encourages foreign investment in the automobile sector and allows 100 per cent FDI under the automatic route. To boost manufacturing, the government had lowered excise duty on small cars, motorcycles, scooters and commercial vehicles to eight per cent from 12 per cent, on sports utility vehicles to 24 per cent from 30 per cent, on mid-segment cars to 20 per cent from 24 per cent and on large-segment cars to 24 per cent from 27 per cent.

The government's decision to resolve VAT disputes has also resulted in the top Indian auto makers namely, Volkswagen, Bajaj Auto, Mahindra & Mahindra and Tata Motors announcing an investment of around Rs 11,500 crore (US$ 1.87 billion) in Maharashtra.

The Automobile Mission Plan for the period 2006–2016, designed by the government is aimed at accelerating and sustaining growth in this sector. Also, the well-established Regulatory Framework under the Ministry of Shipping, Road Transport and Highways, plays a part in providing a boost to this sector.

The Government of India-appointed SIAM and Automotive Components Manufacturers Association (ACMA) are responsible in working for the development of the Indian automobile industry.

Road Ahead

The future of the auto industry depends on the positive sentiments and the demand for vehicles in the market. With the festival season coming up, the Indian auto sector will see a rise in demand which is expected to bring in major growth. An auto dealer survey by firm UBS suggested that the Indian auto industry, riding on trends like the upcoming festival season and decline in fuel price, will observe a 12 per cent y-o-y growth in FY15. Also, keeping up with international trends, there is expected to be a surge in the number of hybrid vehicles in the Indian auto sector in the years to come. Exchange Rate Used: INR 1 = US$ 0.0163 as on October 28, 2014.

A Multinational automobile company "Tivata Cars" want to enter the Indian market. Perform Porter's Five Forces analysis for the company.

Hints:

Threat of new entry	**Supplier power**
■ Large amount of capital required	■ Large number of suppliers
■ High retaliation possible from existing companies, if new entrants would bring innovative products and ideas to the industry	■ Some suppliers are large but the most of them are pretty small
■ Few legal barriers protect existing companies from new entrants	■ Companies use another type of material (use one metal instead of another) but only to some extent (plastic instead of metal)
■ All automotive companies have established brand image and reputation	■ Materials widely accessible
■ Products are mainly differentiated by design and engineering quality	■ Suppliers do not pose any threat of forward integration
■ New entrant could easily access suppliers and distributors	
■ A firm has to produce at least 5 million (by some estimations) vehicles to be cost competitive, therefore it is very hard to achieve economies of scale	
■ Governments often protect their home markets by introducing high import taxes	
Buyer power	**Threat of substitutes**
■ There are many buyers	■ There are many alternative types of transportation, such as bicycles, motorcycles, trains, buses or planes
■ Most of the buyers are individuals that buy one car, but corporates or governments usually buy large fleets and can bargain for lower prices	■ Substitutes can rarely offer the same convenience
■ It doesn't cost much for buyers to switch to another brand of vehicle or to start using other type of transportation	■ Alternative types of transportation almost always cost less and sometimes are more environment friendly
■ Buyers can easily choose alternative car brand	

■ Buyers are price sensitive and their decision is often based on how much does a vehicle cost ■ Buyers do not threaten backward integration	

Competitive rivalry

- Moderate number of competitors
- If a firm would decide to leave an industry it would incur huge losses, so most of the time it either bankrupts or stays in automotive industry for the lifetime
- Industry is very large but matured
- Size of competing firm's vary but they usually compete for different consumer segments
- Customers are loyal to their brands
- There is moderate threat of being acquired by a competitor

5. GLOBAL COMPETITIVENESS INDEX

Introduction

The World Economic Forum releases annual Global Competitiveness Reports which studies and benchmarks the many factors underpinning national competitiveness. The goal is to provide insight and stimulate the discussion among all stakeholders on the best strategies and policies to help countries to overcome the obstacles to improving competitiveness. The Global Competitiveness Report series has evolved over the last three decades into the world's most comprehensive assessment of national competitiveness. The Report presents the rankings of the Global Competitiveness Index (GCI), developed by Professor Xavier Sala-i-Martín and introduced in 2005. The GCI is based on 12 pillars of competitiveness, providing a comprehensive picture of the competitiveness landscape in countries around the world at different stages of economic development. The Report contains detailed profiles highlighting competitive strengths and weaknesses for each of the 144 economies featured, as well as an extensive section of data tables displaying relative rankings for more than 100 variables.

Since 2005, the World Economic Forum has based its competitiveness analysis on the Global Competitiveness Index (GCI), a comprehensive tool that measures the microeconomic and macroeconomic foundations of national competitiveness. Competitiveness has been defined "as the set of institutions, policies, and factors that determine the level of productivity of a country". The level of productivity, in turn, sets the level of prosperity that can be earned by an economy. The productivity level also determines the rates of return obtained by investments in an economy, which in turn are the fundamental drivers of its growth rates. In other words, a more competitive economy is one that is likely to sustain growth. The concept of competitiveness thus involves static and dynamic components. Although the productivity of a country determines its ability to sustain a high level of income, it is also one of the central determinants of its returns to investment, which is one of the key factors explaining an economy's growth potential.

The 12 Pillars of Competitiveness

Many determinants drive productivity and competitiveness. Understanding the factors behind this process has occupied the minds of economists for hundreds of years, engendering theories ranging from Adam Smith's focus on specialization and the division of labor to neoclassical economists' emphasis on investment in physical capital and infrastructure, and, more recently, to interest in other mechanisms such as education and training, technological progress, macroeconomic stability, good governance, firm sophistication, and market efficiency, among others. While all of these factors are likely to be important for competitiveness and growth, they are not mutually exclusive – two or more of them can be significant at the same time, and in fact that is what has been

shown in the economic literature. This open-endedness is captured within the GCI by including a weighted average of many different components, each measuring a different aspect of competitiveness. These components are grouped into 12 pillars of competitiveness (see Figure at the end of the topic):

1. First pillar: Institutions: The institutional environment is determined by the legal and administrative framework within which individuals, firms, and governments interact to generate wealth. The importance of a sound and fair institutional environment became even more apparent during the recent economic and financial crisis and is especially crucial for further solidifying the fragile recovery given the increasing role played by the state at the international level and for the economies of many countries. The quality of institutions has a strong bearing on competitiveness and growth. It influences investment decisions and the organisation of production and plays a key role in the ways in which societies distribute the benefits and bear the costs of development strategies and policies. For example, owners of land, corporate shares, or intellectual property are unwilling to invest in the improvement and upkeep of their property if their rights as owners are not protected. The role of institutions goes beyond the legal framework. Government attitudes toward markets and freedoms and the efficiency of its operations are also very important: excessive bureaucracy and red tape, overregulation, corruption, dishonesty in dealing with public contracts, lack of transparency and trustworthiness, inability to provide appropriate services for the business sector, and political dependence of the judicial system impose significant economic costs to businesses and slow the process of economic development. In addition, the proper management of public finances is also critical to ensuring trust in the national business environment. Indicators capturing the quality of government management of public finances are therefore included here to complement the measures of macroeconomic stability captured in pillar 3 below. Although the economic literature has focused mainly on public institutions, private institutions are also an important element in the process of creating wealth. The recent global financial crisis, along with numerous corporate scandals, have highlighted the relevance of accounting and reporting standards and transparency for preventing fraud and mismanagement, ensuring good governance, and maintaining investor and consumer confidence. An economy is well served by businesses that are run honestly, where managers abide by strong ethical practices in their dealings with the government, other firms, and the public at large. Private-sector transparency is indispensable to business, and can be brought about through the use of standards as well as auditing and accounting practices that ensure access to information in a timely manner.

2. Second pillar: Infrastructure: Extensive and efficient infrastructure is critical for ensuring the effective functioning of the economy, as it is an important factor in determining the location of economic activity and the kinds of activities or sectors that can develop in a particular instance. Well-developed infrastructure reduces the effect of distance between regions, integrating the national market and connecting it at low cost to markets in other countries and regions. In addition, the quality and extensiveness of infrastructure networks significantly impact economic growth and reduce income inequalities and poverty in a variety of ways. A well-developed transport and communications infrastructure network is a prerequisite for the access of less-developed communities to core economic activities and services. Effective modes of transport – including quality roads, railroads, ports, and air transport – enable entrepreneurs to get their goods and services to market in a secure and timely manner and facilitate the movement of workers to the most suitable jobs. Economies also depend on electricity supplies that are free of interruptions and shortages so that businesses and factories can work unimpeded. Finally, a solid and extensive telecommunications network allows for a rapid and free flow of information, which increases overall economic efficiency by helping to ensure that businesses can communicate and decisions are made by economic actors taking into account all available relevant information.

3. Third pillar: Macroeconomic environment: The stability of the macroeconomic environment is important for business and, therefore, is important for the overall competitiveness of a country.10 Although it is certainly true that macroeconomic stability alone cannot increase the productivity of a nation, it is also recognized that macroeconomic instability harms the economy, as we have seen over the past years, notably in the European context. The government cannot provide services efficiently if it has to make high-interest payments on its past debts. Running fiscal deficits limits the government's future ability to react to business cycles and to invest in

competitiveness-enhancing measures. Firms cannot operate efficiently when inflation rates are out of hand. In sum, the economy cannot grow in a sustainable manner unless the macro environment is stable. Macroeconomic stability has captured the attention of the public most recently when some European countries needed the support of the IMF and other euro zone economies to prevent sovereign default, as their public debt reached unsustainable levels. It is important to note that this pillar evaluates the stability of the macroeconomic environment, so it does not directly take into account the way in which public accounts are managed by the government. This qualitative dimension is captured in the institutions pillar described above.

4. Fourth pillar: Health and primary education: A healthy workforce is vital to a country's competitiveness and productivity. Workers who are ill cannot function to their potential and will be less productive. Poor health leads to significant costs to business, as sick workers are often absent or operate at lower levels of efficiency. Investment in the provision of health services is thus critical for clear economic, as well as moral, considerations. In addition to health, this pillar takes into account the quantity and quality of the basic education received by the population. Basic education increases the efficiency of each individual worker. Moreover, workers who have received little formal education can carry out only simple manual tasks and find it much more difficult to adapt to more advanced production processes and techniques, and therefore contribute less to come up with or execute innovations. In other words, lack of basic education can become a constraint on business development, with firms finding it difficult to move up the value chain by producing more sophisticated or value-intensive products with existing human resources. For the longer term, it will be essential to avoid significant reductions in resource allocation to these critical areas, in spite of the fact that government budgets will need to be cut to reduce the deficits and debt burden.

5. Fifth pillar: Higher education and training: Quality higher education and training is particularly crucial for economies that want to move up the value chain beyond simple production processes and products. In particular, today's globalizing economy requires countries to nurture pools of well-educated workers who are able to perform complex tasks and adapt rapidly to their changing environment and the evolving needs of the economy. This pillar measures secondary and tertiary enrollment rates as well as the quality of education as evaluated by the business community. The extent of staff training is also taken into consideration because of the importance of vocational and continuous on-the-job training – which is neglected in many economies – for ensuring a constant upgrading of workers' skills.

6. Sixth pillar: Goods market efficiency: Countries with efficient goods markets are well positioned to produce the right mix of products and services given their particular supply-and-demand conditions, as well as to ensure that these goods can be most effectively traded in the economy. Healthy market competition, both domestic and foreign, is important in driving market efficiency and thus business productivity by ensuring that the most efficient firms, producing goods demanded by the market, are those that thrive. The best possible environment for the exchange of goods requires a minimum of impediments to business activity through government intervention. For example, competitiveness is hindered by distortionary or burdensome taxes and by restrictive and discriminatory rules on foreign direct investment (FDI) – limiting foreign ownership – as well as on international trade. The recent economic crisis has highlighted the degree of interdependence of economies worldwide and the degree to which growth depends on open markets. Protectionist measures are counterproductive as they reduce aggregate economic activity. Market efficiency also depends on demand conditions such as customer orientation and buyer sophistication. For cultural or historical reasons, customers may be more demanding in some countries than in others. This can create an important competitive advantage, as it forces companies to be more innovative and customer-oriented and thus imposes the discipline necessary for efficiency to be achieved in the market.

7. Seventh pillar: Labor market efficiency: The efficiency and flexibility of the labor market are critical for ensuring that workers are allocated to their most effective use in the economy and provided with incentives to give their best effort in their jobs. Labor markets must therefore have the flexibility to shift workers from one economic activity to another rapidly and at low cost, and to allow for wage fluctuations without much

social disruption. The importance of well-functioning labor markets has been dramatically highlighted by last year's events in Arab countries, where rigid labor markets were an important cause of high youth unemployment, sparking social unrest in Tunisia that then spread across the region. Youth unemployment is also high in a number of European countries, where important barriers to entry into the labor market remain in place. Efficient labor markets must also ensure a clear relationship between worker incentives and their efforts to promote meritocracy at the workplace, and they must provide equity in the business environment between women and men. Taken together these factors have a positive effect on worker performance and the attractiveness of the country for talent, two aspects that are growing more important as talent shortages loom on the horizon.

8. Eighth pillar: Financial market development: The recent economic crisis has highlighted the central role of a sound and well-functioning financial sector for economic activities. An efficient financial sector allocates the resources saved by a nation's citizens, as well as those entering the economy from abroad, to their most productive uses. It channels resources to those entrepreneurial or investment projects with the highest expected rates of return rather than to the politically connected. A thorough and proper assessment of risk is therefore a key ingredient of a sound financial market. Business investment is also critical to productivity. Therefore economies require sophisticated financial markets that can make capital available for private-sector investment from such sources as loans from a sound banking sector, well-regulated securities exchanges, venture capital, and other financial products. In order to fulfill all those functions, the banking sector needs to be trustworthy and transparent, and – as has been made so clear recently – financial markets need appropriate regulation to protect investors and other actors in the economy at large.

9. Ninth pillar: Technological readiness: In today's globalized world, technology is increasingly essential for firms to compete and prosper. The technological readiness pillar measures the agility with which an economy adopts existing technologies to enhance the productivity of its industries, with specific emphasis on its capacity to fully leverage information and communication technologies (ICT) in daily activities and production processes for increased efficiency and enabling innovation for competitiveness.14 ICT has evolved into the "general purpose technology" of our time,15 given the critical spillovers to the other economic sectors and their role as industry-wide enabling infrastructure. Therefore ICT access and usage are key enablers of countries' overall technological readiness. Whether the technology used has or has not been developed within national borders is irrelevant for its ability to enhance productivity. The central point is that the firms operating in the country need to have access to advanced products and blueprints and the ability to absorb and use them. Among the main sources of foreign technology, FDI often plays a key role, especially for countries at a lower stage of technological development. It is important to note that, in this context, the level of technology available to firms in a country needs to be distinguished from the country's ability to conduct blue-sky research and develop new technologies for innovation that expand the frontiers of knowledge. That is why we separate technological readiness from innovation, captured in the 12th pillar, described below.

10. Tenth pillar: Market size: The size of the market affects productivity since large markets allow firms to exploit economies of scale. Traditionally, the markets available to firms have been constrained by national borders. In the era of globalization, international markets can to a certain extent substitute for domestic markets, especially for small countries. Vast empirical evidence shows that trade openness is positively associated with growth. Even if some recent research casts doubts on the robustness of this relationship, there is a general sense that trade has a positive effect on growth, especially for countries with small domestic markets. The case of the European Union illustrates the importance of the market size for competitiveness, as important efficiency gains were realized through closer integration. Although the reduction of trade barriers and the harmonization of standards within the European Union have contributed to raising exports within the region, many barriers to a true single market, in particular in services, remain in place and lead to important border effects. Therefore we continue to use the size of the national domestic and foreign market in the Index. Thus exports can be thought of as a substitute for domestic demand in determining the size of the market for the firms of a country. By including both domestic and foreign markets in our measure of market size, we give credit to export-driven

economies and geographic areas (such as the European Union) that are divided into many countries but have a single common market.

11. Eleventh pillar: Business sophistication: There is no doubt that sophisticated business practices are conducive to higher efficiency in the production of goods and services. Business sophistication concerns two elements that are intricately linked: the quality of a country's overall business networks and the quality of individual firms' operations and strategies. These factors are particularly important for countries at an advanced stage of development when, to a large extent, the more basic sources of productivity improvements have been exhausted. The quality of a country's business networks and supporting industries, as measured by the quantity and quality of local suppliers and the extent of their interaction, is important for a variety of reasons. When companies and suppliers from a particular sector are interconnected in geographically proximate groups, called clusters, efficiency is heightened, greater opportunities for innovation in processes and products are created, and barriers to entry for new firms are reduced. Individual firms' advanced operations and strategies (branding, marketing, distribution, advanced production processes, and the production of unique and sophisticated products) spill over into the economy and lead to sophisticated and modern business processes across the country's business sectors.

12. Twelfth pillar: Innovation: Innovation can emerge from new technological and non technological knowledge. Non-technological innovations are closely related to the know-how, skills, and working conditions that are embedded in organisations and are therefore largely covered by the eleventh pillar of the GCI. The final pillar of competitiveness focuses on technological innovation. Although substantial gains can be obtained by improving institutions, building infrastructure, reducing macroeconomic instability, or improving human capital, all these factors eventually seem to run into diminishing returns. The same is true for the efficiency of the labor, financial, and goods markets. In the long run, standards of living can be largely enhanced by technological innovation. Technological breakthroughs have been at the basis of many of the productivity gains that our economies have historically experienced. These range from the industrial revolution in the 18th century and the invention of the steam engine and the generation of electricity to the more recent digital revolution. The latter is transforming not only the way things are being done, but also opening a wider range of new possibilities in terms of products and services. Innovation is particularly important for economies as they approach the frontiers of knowledge and the possibility of generating more value by only integrating and adapting exogenous technologies tends to disappear. Although less-advanced countries can still improve their productivity by adopting existing technologies or making incremental improvements in other areas, for those that have reached the innovation stage of development this is no longer sufficient for increasing productivity. Firms in these countries must design and develop cutting-edge products and processes to maintain a competitive edge and move toward higher value-added activities. This progression requires an environment that is conducive to innovative activity and supported by both the public and the private sectors. In particular, it means sufficient investment in research and development (R&D), especially by the private sector; the presence of high-quality scientific research institutions that can generate the basic knowledge needed to build the new technologies; extensive collaboration in research and technological developments between universities and industry; and the protection of intellectual property, in addition to high levels of competition and access to venture capital and financing that are analyzed in other pillars of the Index. In light of the recent sluggish recovery and rising fiscal pressures faced by advanced economies, it is important that public and private sectors resist pressures to cut back on the R&D spending that will be so critical for sustainable growth going into the future.

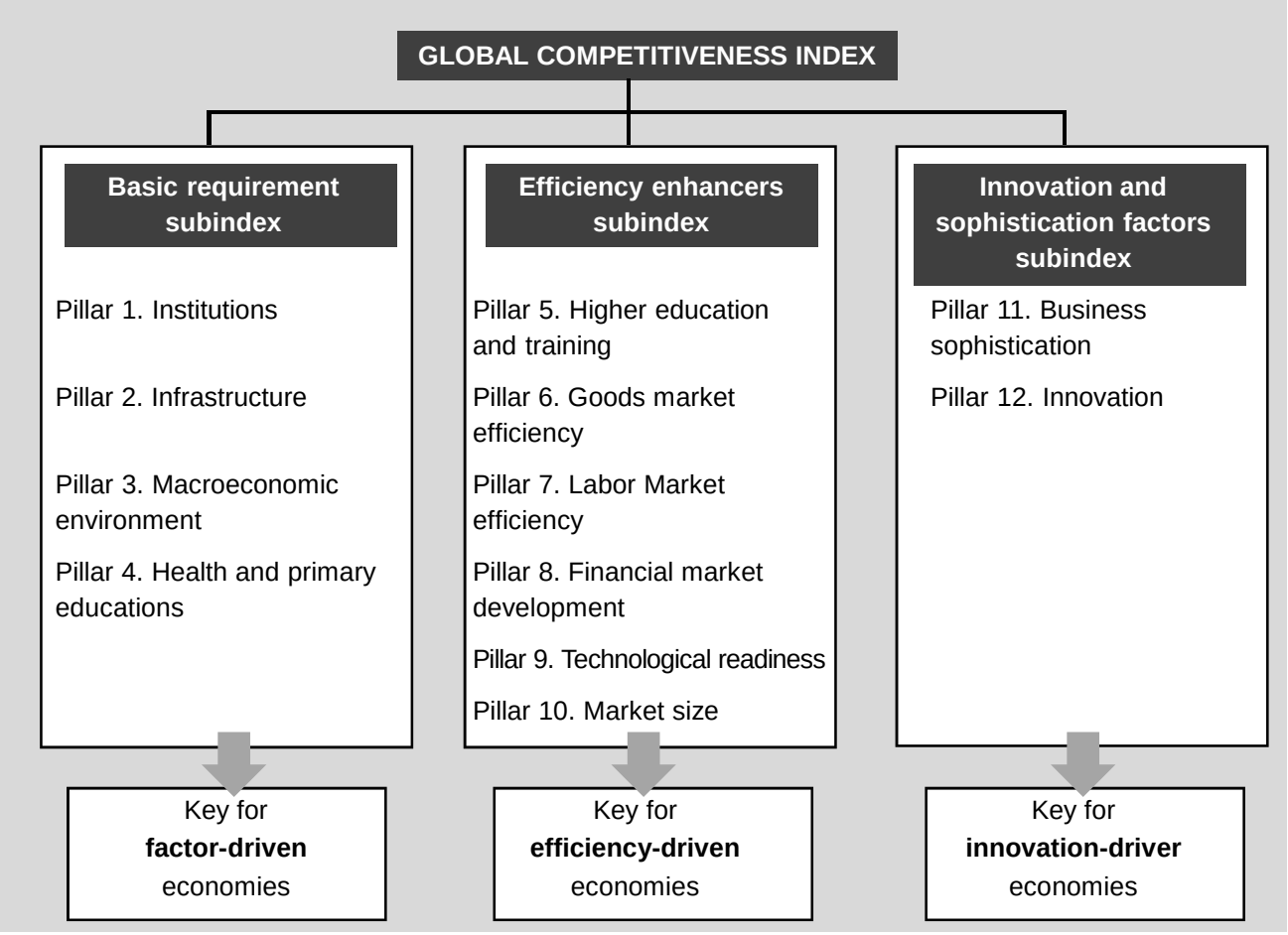
The interrelation of the 12 pillars

While we report the results of the 12 pillars of competitiveness separately, it is important to keep in mind that they are not independent: they tend to reinforce each other, and a weakness in one area often has a negative impact in others. For example, a strong innovation capacity (pillar 12) will be very difficult to achieve without a healthy, well-educated and trained workforce (pillars 4 and 5) that is adept at absorbing new technologies (pillar 9), and without sufficient financing (pillar 8) for R&D or an efficient goods market that makes it possible to take new innovations to market (pillar 6). Although the pillars are aggregated into a single index, measures are reported

for the 12 pillars separately because such details provide a sense of the specific areas in which a particular country needs to improve. The appendix describes the exact composition of the GCI and technical details of its construction.

Stages of development and the weighted index

While all of the pillars described above will matter to a certain extent for all economies, it is clear that they will affect them in different ways: the best way for Cambodia to improve its competitiveness is not the same as the best way for France to do so. This is because Cambodia and France are in different stages of development: as countries move along the development path, wages tend to increase and, in order to sustain this higher income, labor productivity must improve. In line with the economic theory of stages of development, the GCI assumes that economies in the first stage are mainly factor-driven and compete based on their factor endowments – primarily low-skilled labor and natural resources.19 Companies compete on the basis of price and sell basic products or commodities, with their low productivity reflected in low wages. Maintaining competitiveness at this stage of development hinges primarily on well-functioning public and private institutions (pillar 1), a well-developed infrastructure (pillar 2), a stable macroeconomic environment (pillar 3), and a healthy workforce that has received at least a basic education (pillar 4). As a country becomes more competitive, productivity will increase and wages will rise with advancing development. Countries will then move into the efficiency-driven stage of development, when they must begin to develop more efficient production processes and increase product quality because wages have risen and they cannot increase prices.



The Global Competitiveness Index (GCI) 2013-14 Rankings

The GCI as in previous years, this year's top 10 remain dominated by a number of European countries, with Switzerland, Finland, Germany, Sweden, the Netherlands, and the United Kingdom confirming their places among the most competitive economies. Three Asian countries also figure in top 10, with Singapore remaining the second-most competitive economy in the world, and Hong Kong SAR and Japan placing 7th and 9th. It is worth noting that a vast majority of the top 10 most competitive economies share strengths in innovation and a strong institutional framework.

The Global Competitiveness Index (GCI) of India 2013-14

Down one position, India now ranks 60th, continuing its downward trend that began in 2009. With a GCI score essentially unchanged since then, India has been overtaken by a number of countries. Once ahead of Brazil and South Africa, it now trails them by several places and is behind China by a margin of 31 positions, while Russia (64th) has almost closed the gap. India continues to be penalized for its very disappointing performance in the basic drivers underpinning competitiveness, the very ones that matter the most for India given its stage of development. The country's supply of transport, ICTs, and energy infrastructure remains largely insufficient and ill-adapted to the needs of the economy (85th), despite the steady improvement that has been made since 2006. The Indian business community repeatedly cites infrastructure as the single biggest hindrance to doing business, ahead of corruption and cumbersome bureaucracy. Notwithstanding improvements across the board over the past few years, very poor public health and education levels (102nd) remain a prime cause of India's low productivity. The quality of higher education is better, but enrolment rates at that level remain very low, even by developing country standards. Turning to the country's institutions (72nd, down two places), discontent within the business community remains high about the lack of reforms and the perceived inability of the government to push them through. Public trust in politicians has been eroding since 2009 and has now reached an all-time low at 115th, while bribery remains deeply rooted (110th). Indeed, India has lost almost 30 ranks on this indicator since 2010. Meanwhile, the situation has deteriorated further on the macroeconomic front, with India now 110th in this pillar. The inflation rate and public deficit-to-GDP ratio were dangerously close to double digits in 2012, and the debt-to- GDP ratio is the second highest among the BRICS. Indeed, a March 2013 survey of sovereign debt analysts reveals an increased risk of sovereign debt default over the previous year. Another major concern is the country's low level of technological readiness (98th). Although businesses adopt new technologies relatively promptly (47th), penetration rates of fixed and mobile Internet and telephony among the population remain among the lowest in developing Asia. Furthermore, the situation has worsened in terms of labor market efficiency (99th), where the most salient problem remains the dismally low participation of women in the workforce. With a ratio women-to-men of 0.36 (137th), India has the lowest percentage of working women outside the Arab world.

LESSON ROUND UP

- PEST analysis is an analysis of the political, economic, social and technological factors in the external environment of an organisation, which can affect its activities and performance.
- SWOT analysis is an analysis of an organisation's strengths and weaknesses alongside the opportunities and threats present in the external environment.
- Porter's five forces model is an analysis tool that uses five forces to determine the profitability of an industry and shape a firm's competitive strategy. It is a framework that classifies and analyzes the most important forces affecting the intensity of competition in an industry and its profitability level. Five forces model was created by M. Porter in 1979 to understand how five key competitive forces are affecting an industry.
- The Global Competitiveness Index (GCI), a comprehensive tool that measures the microeconomic and macroeconomic foundations of national competitiveness. Competitiveness has been defined "as the set of institutions, policies, and factors that determine the level of productivity of a country".

SELF TEST QUESTIONS

1. What do you mean by international business environment? Explain internal and external business environment.
2. How economic environment affects the international business? Explain citing real examples.
3. Technology has become very important nowadays. How technological environment affects business decisions in global world?
4. Do the PEST analysis of an Indian FMCG company. Also try to apply other variations of PEST like PESTEL and STEEPLE analysis
5. Explain SWOT analysis. Do the SWOT analysis of a multinational company in retail sector.
6. Explain briefly Porter's Five Forces Model for assessing competitiveness of an organisation in global environment.
7. What is global competitiveness index? Explain the pillars of GCI and how is it calculated?

Lesson 3
Multinational Enterprises (MNEs) and Foreign Direct Investments (FDI)

LESSON OUTLINE

Multinational Enterprises/Corporations
- Meaning and Definition
- Characteristics of Multinational Corporations
- Forms of Multinational Corporations
- Role of Multinational Corporations
- Criticism of Multinational Corporations
- Issues with Multinational Corporations

Foreign Direct Investment
- Meaning and Definition
- Importance of FDI
- Advantages of FDI
- Disadvantages of FDI
- Industrial Policy of India
  - Industrial Policy Resolution, 1948
  - Industrial Policy Resolution, 1956
  - New Industrial Policy, 1991
- FDI policy framework in India
- Role of Department of Industrial Policy & Promotion
- Consolidated FDI Policy of India
- Foreign Investment Implementation Authority (FIIA)
- Case Study on FDI policy: The International Experience
- Case Study on Cross-country Comparison of FDI policies
- LESSON ROUND UP
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

Multinational corporations (MNCs) play a large and growing role in shaping our world, both economically and politically. Multinational corporations are important factors in the processes of globalization. National and local governments often compete against one another to attract MNC facilities, with the expectation of increased tax revenue, employment, and economic activity. MNCs play an important role in developing the economies of developing countries like investing in these countries provide not only market to the MNCs but also provide employment, choice of multi goods etc. to the consumers. MNCs account for over half of the industrial output of the world. The names of some of the largest MNCs include Wal-mart, General Motors, Exxon-Mobil, Mitsubishi, Siemens, etc.

Foreign Direct Investment (FDI) is a direct investment into production or business in a country by a company in another country, either by buying a company in the target country or by expanding operations of an existing business in that country. Foreign direct investment is in contrast to portfolio investment which is a passive investment in the securities of another country such as stocks and bonds. FDI is a major source of getting foreign exchange. All countries in the world try to attract foreign investment through attractive FDI policy.

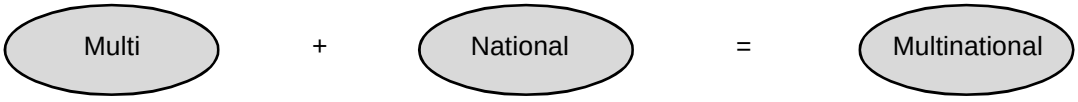
In this chapter we will study about the Multinational corporations, Foreign direct Investment, recent trends in Global FDI and FDI in India and FDI policy of India.

Foreign Direct Investment, or FDI, is a type of investment that involves the injection of foreign funds into an enterprise that operates in a different country of origin from the investor.

MULTINATIONAL ENTERPRISES / MULTINATIONAL CORPORATIONS

Meaning and Definition

International business describes bussines or operations of firms having interests in multiple countries. Such firms are called multinational corporations (MNCs). Some of the as well known MNCs include fast food companies like McDonald's and Yum Brands, vehicle manufacturers such as General Motors and Toyota, consumer electronics companies like Samsung, LG and Sony, and energy companies such as Exxon Mobil and BP. Most of the largest corporations operate in multiple national markets.



The term 'multinational' consists of two different words, multi and national. The prefix multi here means many while the word national refers to nations or countries. Therefore, a multinational company may be defined as a company that operates in several countries. Such a company has factories, branches or offices in more than one country. According to the United Nations Commission on Transnational Corporations, a transnational corporation is a corporation which operates, in addition to the country in which it is incorporated, in one or more countries.

Definition of Multinational Corporation – MNC is a corporation that has its facilities and other assets in at least one country other than its home country. Such companies have offices and/or factories in different countries and usually have a centralized head office where they co-ordinate global management.

The operations of a Multinational Corporation (MNC) extend beyond the country in which it is incorporated. Its headquarters are located in one country (home country) and in addition it carries on business in other countries (host country). For example, Coca Cola Corporation has its headquarters in the U.S.A. and it has branches/ subsidiaries in several countries. A multinational corporation controls production and marketing facilities in more than one country. Firms that participate in international business, however, large they may be, solely by exporting or by licensing technology are not multinational corporations. Nearly all major multinationals are American, Japanese or Western European, such as Nike, Coca-Cola, Wal-Mart, AOL, Toshiba, Honda and BMW.

The terms 'multinational corporation', international corporation', transnational corporation', and 'global corporation' are often used interchangeably. But some experts make a distinction between these terms.

Multinational Corporation	– A 'Multinational Corporation' is a company which operates in several countries and a considerable share of its business is from foreign countries.
International Corporation	– An 'International Corporation' may be defined as a company which has business operations in at least one foreign country.
Transnational Corporation	– A 'Transnational Corporation' is a multinational, the ownership and control of which are dispersed internationally. It has no principal domicile and no single central source of power. Unilever, Shell and Royal Dutch are examples of transnational corporation.
Global Corporation	– A 'Global Corporation' is a company which views the entire world as a single homogenous market and caters to the global market through globally standardized products.

CHARACTERISTICS OF MULTINATIONAL CORPORATIONS

- Giant Size
- International Operations
- Centralized Control
- Oligopolistic Power
- Sophisticated Technology
- Professional Management
- International Market
- Multiple objectives

The salient features of multinational corporations are as follows:

(i) Giant Size: The assets and sales of a multinational are quite large. The sales turnover of some MNCs exceed the Gross National Product of several developing countries. For example, the physical assets of International Business Machines (IBM) exceed $ 8 billion dollars.

(ii) International Operations: A multinational corporation has production, marketing and other facilities in several countries. It operations through a network of subsidiaries, branches and affiliates in host countries. It operates through a network of subsidiaries, branches and affiliates in host countries. It owns and controls assets in foreign countries. For example, ITI has about 800 subsidiaries in more than 70 countries.

(iii) Centralized Control: A multinational corporation has its headquarters in the home country. It exercises control over all branches and subsidiaries. The local managements of branches and subsidiaries operate within the policy framework of the parent corporation.

(iv) Oligopolistic Power: Multinational corporations are generally oligopolistic in nature. Due to their giant size they occupy a dominant position in the market. They also take over other firms to acquire a huge economic power. For example, Hindustan Lever Limited acquired Tata Oils Mills.

(v) Sophisticated Technology: Generally, a multinational corporation has at its command advanced technology so as to provide world class products and services. It employs capital intensive technology not only in manufacturing but in marketing and other areas of business

(vi) Professional Management: In order to integrate and manage worldwide operations, a multinational corporation employs professional skills. It employs professionally trained managers to handle advanced technology, huge funds and international business operations.

(vii) International Market: On account of its vast resources and superior marketing skills, a multinational corporation has vast access to international markets. Therefore, it is able to sell whatever product/ service it produces in different countries.

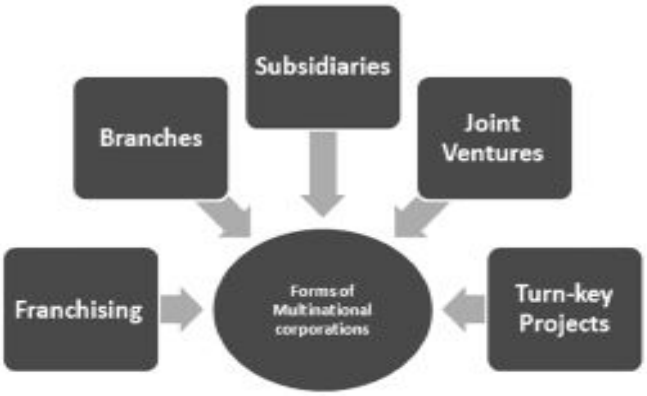
(viii) Multiple objectives: Multinational corporations make investments in different countries with the following aims:

- to take advantage of tax benefits in host countries or to circumvent tariff barriers;
- to exploit the natural resources of the host country;
- to take advantage of Government concessions in host countries
- to mitigate the impact of regulations in the home country;
- to reduce costs of production by making use of cheap labour and lower transportation expenses in host countries;

– to gain dominance in foreign markets;

– to expand activities vertically.

Forms of Multinational Corporations



(i) Franchising : In this form, a multinational corporation grants firms in foreign countries the right (franchise) to use its trade marks, brand names, patents, technology, etc. The firms getting the right or license operate as per the terms and conditions of the franchise agreement. They pay a periodical royalty or license fee to the multinational corporation. In case the firm, holding franchise violate the terms of the agreement, the license may be cancelled. This system is popular for products which enjoy good demand in host countries.

(ii) Branches : A multinational corporation may open branches in different countries. These branches work under the direction and control of the head office. The headquarters lay down policy guideline to be followed by the branches. Every branch follows the laws and regulations of the country in which it is located. Multinationals find it easiest to operate through branches.

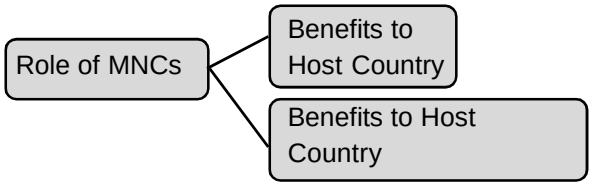
(iii) Subsidiaries : A multinational corporation may establish wholly owned subsidiaries in foreign countries. In case of partly owned subsidiaries people in the host country also own shares. The multinational controls the Board of Directors of the subsidiary company and the subsidiary follows the policies laid down by the parent company. The holding company undertakes responsibility for the management and working of the subsidiaries. Subsidiaries are considered to be more profitable than franchising. A multinational can expand its business operations through subsidiaries all over the world.

(iv) Joint Ventures : In this system**,** a multinational corporation establishes a company in a foreign company in partnership with a local firm for manufacturing or marketing some product. The multinational and foreign firms share the ownership and control of the business. Generally, the multinational provides the technical know-how and managerial expertise whereas day-to-day management is left to the local partner. For example, in Maruti Udyog, the Government of India and Suzuki of Japan have jointly supplied the capital and are sharing profits. Suzuki supplies advanced technology and day-to-day management lies mainly with people nominated by the Government of India. The multinational corporation contributes capital for the joint venture and shares profits as per the agreement.

(v) Turn-key Projects : In this method, the multinational corporation undertakes a project in a foreign country. The multinational constructs and operates an industrial plant from beginning to end. The local client does not participate actively at various stages of construction. The personnel of the corporation have technical expertise in the concerned industry and they may train the client's staff in the operation of the plant. The multinational may guarantee the quantity and quality of production over a long period of time. When the project is complete, it is handed over to the host country. This form is used by under developed countries to complete projects which require high technical skill and experience. Underdeveloped countries invite multinationals to construct huge projects involving technical and managerial expertise and huge financial resources.

ROLE OF MULTINATIONAL CORPORATIONS

Multinational corporations play both positive and negative roles. As a positive force, multinationals can be a dynamic force or instrument for wider distribution of capital, technology and employment. As a negative force, multinationals can be monsters beyond the control of national governments and working against public interest.



Benefits to Host Country

Multinationals can offer the following gains to host countries:

(i) Foreign Capital : Developing countries suffer from shortage of capital required for rapid industrialization. Multinational corporations bring in much needed capital for the development of these countries. These corporations make direct foreign investment thereby speeding up the process of economic development. Since liberalization, India has, for eg: attracted foreign investment worth several billion dollars.

(ii) Advanced Technology : Developing countries are technologically backward. They lack sufficient resources to carry on research and development. Multinationals serve as vehicles for the transfer of advanced technology to these countries. Advanced technological knowhow, improved skills and consultancy help the developing countries to improve the quality of products and reduce costs. Through continuous research and development, MNCs serve as a source of inventions and innovations.

(iii) Employment Generation : Multinationals create large scale employment opportunities in host countries. They increase the investment level and thereby the employment and income levels. Multinationals offer excellent pay scales and career opportunities to managers, technical and clerical staff.

(iv) Foreign Exchange : Multinationals help the host countries to increase their exports and reduce their dependence on imports. As a result, these corporations enable the host economies to improve balance of payment position.

(v) Managerial Revolution : Multinationals help to professionalise management in host countries. They employ modern management techniques and trained managers. Several concepts and techniques like corporate planning, management by objectives and job enrichment were evolved by multinational corporations. As carriers of knowledge and experience, multinationals build up 'knowledge base' and thereby assist the development of human resources in host countries.

(vi) Healthy Competition : Multinationals increase competition and thereby break domestic monopolies. They compel the domestic companies to improve their efficiency or withdraw from the market. For example, many Indian companies acquired ISO-9000 quality certification due to competition from multinational corporations after liberalization.

(vii) Growth of Domestic Firms : MNCs stimulate the growth of local enterprises. In order to support its other operations, a multinational may assist domestic suppliers and ancillary units.

(viii) Standard of Living : By providing superior products and services, MNCs help to improve living standards in host countries.

(ix) World Economy : MNCs help to integrate national economies into a world economy. They encourage international brotherhood and cultural exchanges through international business.

Benefits to Home Country

Multinationals offer the following advantages to the country of their origin :

(i) The home country can obtain raw materials and labour at comparatively lower cost.

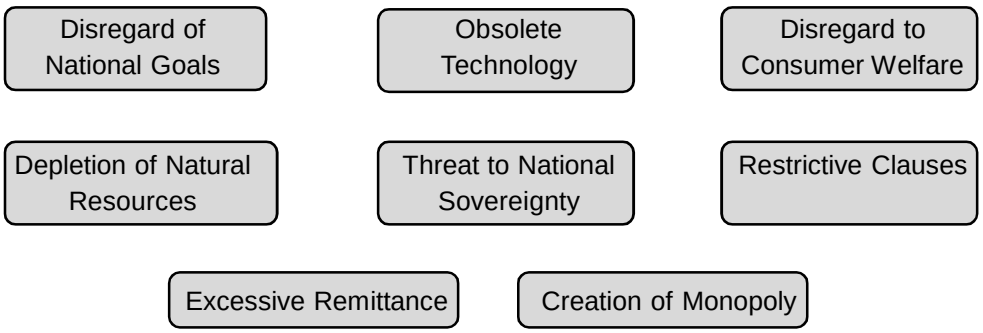
(ii) It can export components and finished products and thereby market is widened.

(iii) It can earn huge revenue by way of dividends, royalty, licensing fees, etc.

(iv) It can increase domestic employment due to higher scale of operations.

(v) It can acquire technical and managerial expertise of foreign nations.

CRITICISM OF MULTINATIONAL CORPORATIONS



1. **Disregard of National Goals:** MNCs invest in sectors that are profitable disregarding the goals and priorities of host countries. They do very little for underdeveloped strategic sectors and backward regions. Due to their capital intensive technology and profit-mindedness, they create relatively few jobs and fail to solve the basic problems like unemployment and poverty of host nations.
2. **Obsolete Technology:** MNCs often transfer outdated technology to their collaborators in host countries. In many cases technology transferred is unsuitable causing waste of scarce capital. Repetitive imports of similar technology leads to excessive royalty payments without adding to technical knowledge in host countries. Sometimes, imported machinery remains idle for want of repairs and maintenance facilities. MNCs have failed to develop local skills and talents. MNCs use capital intensive technology which may reduce jobs.
3. **Excessive Remittance:** MNCs squeeze out maximum payment from their subsidiaries/affiliates and collaborators in the form of royalty, technical fee, dividend, etc. By repatriating profits, MNCs put severe pressures on the foreign exchange reserves and balance of payments of host countries.
4. **Creation of Monopoly:** MNCs join hands with big business houses and give rise to monopoly and concentration of economic power in host countries. They kill indigenous enterprises through strategic advantages like patents, superior technology, etc. For example, Pearl Soft Drinks and Kwality Ice Cream Co., had to sell themselves to foreign MNCs in India. MNCs pose a threat to small scale industries.
5. **Restrictive Clauses:** Due to their strong bargaining power, MNCs introduce restrictive clauses in collaboration agreements, e.g., technology cannot be passed to third parties, pricing of products will be by the MNC, exports from host country will be restricted and managerial posts will be filled by parent company. MNCs do not transfer R&D, training and other facilities to host countries.
6. **Threat to National Sovereignty:** MNC pose a danger to the independence of host countries. These corporations tend to interfere in the political affairs of host nations. Some MNCs like ITI are accused of overthrowing Governments in countries such as Chile.

7. **Depletion of Natural Resources :** MNC cause rapid depletion of some of the non-renewable natural resources in host countries.

8. **Disregard to Consumer Welfare** : Their main objective of coming to India is to exploit the big market available here. Most of them are in FMCG selling fast food (junk food) with no nutritive value e.g., Pepsi Co. and Coca-Cola selling soft drinks and snacks, Nestle, McDonald.

Issues with Multinational Corporations

1. **Taxation issues:** An MNC in its true sense operates with different companies located in different countries under same management group. They transfer finished and semi-finished goods, raw materials, spares and services among the group companies. 40% of the international trade consists of transfers between related business companies. For MNCs there are the separate tax and tariffs rates, government regulations but they have to operate under political risk as compared to their domestic counter parts. Transfer pricing helps an MNC in tax planning, avoiding exchange controls and supporting credit status of affiliates. In many cases, there are chanres against MNCs on the usage of transfer pricing system for dubious activities. Hence, it becomes a source of conflict between the MNC and the host government. However, the adverse effects of transfer pricing can be checked to a great extent by regulations. As per one school of thought there should not be any regulation for transfer pricing and no MNC will be compelled to adopt transfer pricing technique. The play of market force will decide optimal allocation of resources. However this concept is not quite prevalent and hence, it requires some regulation, which may be direct or indirect. Direct Regulation includes the measures replacing directly one particulars transfer price by another set of prices fixed by the host government. All the intra firm transactions are required to take place at the fixed place. In many developing countries, the government has fixed ceiling on the royalty payment, but that affects adversely to MNCs. In short, it can be said that, direct regulations is possible. Indirect regulation may be applied in different forms, which are as follows:
   - Harmonization of tax and tariff between home and host country,
   - compensation for the loss of corporate tax revenues on account of transfer pricing
   - Apportionment of the consolidated profit of the MNC among the relevant units on the basis of total assets, sales and labour and capital employed
2. **Ethical issues:** Scandals and bankruptcies in the United States at companies like Enron and WorldCom Inc. have focused attention on the abuse of the power entrusted to executives by shareholders, employees and customers and they underscore the need for reforms to bolster business ethics. Corruption is not inherent to any one society. Its reach is global. Fifteen percent of all companies in industrialized nations have to pay bribes to win or retain business. Ethical issues in business have become more complicated because of the global and diversified nature of many large corporations. Managers must balance the ideal against the need to produce a reasonable profit for the company's shareholders with honesty in business practices, safety in the workplace, and larger environmental and social issues.
3. **Cultural issues:** Multinational companies face a number of different cultural problems as they move forward in today's global marketplace. Many of those problems are internal cultural problems, but some may of an external nature also. Given the nature of the global environment, multinational companies will increasingly find themselves having to make decisions that are based on cultural problems created by the global market.
   - ***Diversity*** - One of the main cultural challenges faced by multinational companies is the diversity of cultural perspectives found within the organization. This can cause problems in terms of management and policy development, because it makes it difficult for the organization to make company-wide policy decisions without having to take into consideration the variety of cultural viewpoints represented within the organization itself. In short, as companies move forward in the global context, too much diversity may create problems.

- **Organizational Culture** - Along the same lines as an overabundance of diversity, multinational companies also face the difficult task of developing a unified organizational culture from within. Because of the different cultural perspectives represented within the organization as a whole, company leaders generally face the difficult task of having to create a workplace culture to which all employees can adhere. Concepts of teamwork and unity may have different meanings across the national boundaries, making it far more tricky to develop a unified company perspective.
- **Human Resources** - Companies of a multinational variety will also face problems when it comes to human resources operations. For instance, when it comes to recruiting, human resources managers may find themselves having to overcome cultural barriers to find qualified candidates for positions abroad. In some cases, management professionals may find themselves facing a lack of qualified talent to fill important positions that require advanced degrees and training. Finding employees at home who are qualified or willing to step in and fill such positions in a context outside of their home country may also prove problematic. Some employees may simply not want to serve in certain parts of the world.
- **Sales** - Another problem that multinational companies may face in a global environment is the ability to develop products and market those products in a way that appeals to a wide segment of the world's population. Companies run the risk of developing products and strategies that run contrary to the cultural norms of the people to which they are attempting to market the products. Multinational companies face the challenge of developing and marketing products that have global appeal.
- **Communication and Cultural Norms** - Another significant issue faced by multinational companies is how business is conducted across international lines. Differences in communication, for instance, make it essential to understand cultural norms in the countries in which these companies operate. For instance, John Hooker at Carnegie Melon University points out that some forms of communication have implied and understood meanings that only make sense within a culture's context. This form of "high context communication" requires knowledge of the culture and its understood traditions.
- **Etiquette and Customs** - Multinational companies also have to have representatives and leaders who know how to avoid violating or ignoring cultural practices and customs in business meetings. For instance, sending a woman to conduct business negotiations in the Middle East might be offensive to some Middle Eastern businessmen who typically don't socialize in public with women. In some Asian cultures, bowing, rather than shaking hands, is a more acceptable form of greeting. Other etiquette concerns can include eating customs in business dinners, bringing and giving gifts when appropriate, differences in body language and dress and even methods of negotiation.

FOREIGN DIRECT INVESTMENT (FDI)

Meaning and Definition

Foreign direct investment is an investment made by a company or entity based in one country, into a company or entity based in another country. Foreign direct investments differ substantially from indirect investments such as portfolio flows, wherein overseas institutions invest in equities listed on a nation's stock exchange. Entities making direct investments typically have a significant degree of influence and control over the company into which the investment is made. Open economies with skilled workforces and good growth prospects tend to attract larger amounts of foreign direct investment than closed, highly regulated economies.

Foreign direct investment, in its classic definition, is defined as a company from one country making a physical investment into building a factory in another country. The direct investment in buildings, machinery and equipment is in contrast with making a portfolio investment, which is considered an indirect investment. In recent years, given rapid growth and change in global investment patterns, the definition has been broadened to include the acquisition of a lasting management interest in a company or enterprise outside the investing firm's home country.

For small and medium sized companies, FDI represents an opportunity to become more actively involved in international business activities. In the past 15 years, the classic definition of FDI as noted above has changed considerably. This notion of a change in the classic definition, however, must be kept in the proper context. Very clearly, over 2/3 of direct foreign investment is still made in the form of fixtures, machinery, equipment and buildings. Moreover, larger multinational corporations and conglomerates still make the overwhelming percentage of FDI. But, with the advent of the internet, the increasing role of technology, loosening of direct investment restrictions in many markets and decreasing communication costs means that newer, non-traditional forms of investment will play an important role in the future. Many governments, especially in industrialized and developed nations, pay very close attention to foreign direct investment because the investment flows into and out of their economies can and does have a significant impact.

The investing company may make its overseas investment in a number of ways - either by setting up a subsidiary or associate company in the foreign country, by acquiring shares of an overseas company, or through a merger or joint venture. The accepted threshold for a foreign direct investment relationship, as defined by the OECD, is 10%. That is, the foreign investor must own at least 10% or more of the voting stock or ordinary shares of the investee company.

An example of foreign direct investment would be an American company taking a majority stake in a company in China. Another example would be a Canadian company setting up a joint venture to develop a mineral deposit in Chile.

According to the International Monetary Fund- foreign direct investment, commonly known as FDI, "refers to an investment made to acquire lasting or long-term interest in enterprises operating outside of the economy of the investor." The investment is direct because the investor, which could be a foreign person, company or group of entities, is seeking to control, manage, or have significant influence over the foreign enterprise.

Foreign Direct Investment means "cross border investment made by a resident in one economy in an enterprise in another economy, with the objective of establishing a lasting interest in the investee economy. FDI is also described as "investment into the business of a country by a company in another country". Mostly the investment is into production by either buying a company in the target country or by expanding operations of an existing business in that country". Such investments can take place for many reasons, including to take advantage of cheaper wages, special investment privileges (e.g. tax exemptions) offered by the country.

Importance of FDI

Foreign direct investment (FDI) plays an extraordinary and growing role in global business. It can provide a firm with new markets and marketing channels, cheaper production facilities, access to new technology, products, skills and financing. For a host country or the foreign firm which receives the investment, it can provide a source of new technologies, capital, processes, products, organizational technologies and management skills, and as such can provide a strong impetus to economic development.

FDI is a major source of external finance which means that countries with limited amounts of capital can receive finance beyond national borders from wealthier countries. Exports and FDI have been the two key ingredients in China's rapid economic growth. According to the World Bank, FDI and small business growth are the two critical elements in developing the private sector in lower-income economies and reducing poverty.

In the past decade, FDI has come to play a major role in the internationalization of business. Reacting to changes in technology, growing liberalization of the national regulatory framework governing investment in enterprises, and changes in capital markets profound changes have occurred in the size, scope and methods of FDI. New information technology systems, decline in global communication costs have made management of foreign investments far easier than in the past. The sea change in trade and investment policies and the regulatory

environment globally in the past decade, including trade policy and tariff liberalization, easing of restrictions on foreign investment and acquisition in many nations, and the deregulation and privatisation of many industries, has probably been the most significant catalyst for FDI's expanded role.

Most of the countries seek FDI because of following reasons:

- Domestic capital is inadequate for purpose of economic growth;
- Foreign capital is usually essential, at least as a temporary measure, during the period when the capital market is in the process of development;
- Foreign capital usually brings it with other scarce productive factors like technical know-how, business expertise and knowledge.

Advantages of FDI

- Improves forex position of the country;
- Employment generation and increase in production ;
- Help in capital formation by bringing fresh capital;
- Helps in transfer of new technologies, management skills, intellectual property
- Increases competition within the local market and this brings higher efficiencies
- Helps in increasing exports;
- Increases tax revenues

Disadvantages of FDI

- Domestic companies fear that they may lose their ownership to overseas company;
- Small enterprises fear that they may not be able to compete with world class large companies and may ultimately be edged out of business;
- Large giants of the world try to monopolise and take over the highly profitable sectors;
- Such foreign companies invest more in machinery and intellectual property than in wages of the local people;
- Government has less control over the functioning of such companies as they usually work as wholly owned subsidiary of an overseas company.

Note for students :

- **Students are advised to study and interpret latest trends in global FDI from various reports available on the websites of UNCTAD, OECD, World Bank, IMF, etc.**
- **The FDI statistics and trends in India are available on the websites of RBI.**

INDUSTRIAL POLICY OF INDIA

Industrialization is a major objective of developing countries as a means to the attainment of higher levels of economic well-being of the people. Advancement of science and technology provides the stimulus to achieve faster industrial growth. The process of acquisition of technology involves a sequence of inter-linked activities, such as identification of technological needs in the light of the objectives of economic and social developments, the obtaining of information on alternative sources of technology, including local sources, the dissemination of information on technologies to potential users, the evaluation and selection of most appropriate technology, in

order to assess the suitability, costs and conditions of their components, negotiation of terms and conditions, optimum exploitation and the use of results of exploitation of technology in the country.

After four and half decades of strongly inward oriented policies, India began opening up of its economy to foreign trade and investment with the announcement of New Industrial Policy in July 1991. The New Industrial Policy sought to prepare Indian industry for meeting the challenges of globalization. The reforms aim at generating a market orientation for the hitherto highly regulated domestic economy by deregulating the domestic economy to provide Indian industry with greater flexibility to respond to competitive pressures by reducing costs and improving quality.

The New Industrial Policy has injected a substantial measure of competitive environment and market thrust to industry. Many areas earlier reserved for the public sector are now open to private sector participation. The restrictions on the expansion of large industrial houses have been removed. Licensing requirements for industries have been abolished except for a few strategic and defence industries.

The policy reforms towards Foreign Direct Investment (FDI) began with a radically new approach to FDI in the very first year of the implementation of New Industrial Policy. The new regime permits FDI in virtually every sector of the economy. Foreign equity proposals need not be accompanied by technology transfer as required earlier. Royalty payments have been considerably liberalised, no restrictions on the use of foreign brand name/ trademarks for internal sale.

In view of the major changes introduced in the Indian economy and the liberalization of Industrial and trade policies consistent with the fast changing international economic and trade relations, it has become necessary to create a better and more conducive atmosphere for increased inflow of foreign investment and capital in the country to accelerate industrial growth and promotion of trade, with greater emphasis on export.

Industrial Policy Resolution, 1948

Immediately after independence, the Government gave a careful thought to the economic problems facing India and recognised that any improvement in the economic conditions of the people is possible only through a substantial increase in the generation of national wealth as a mere distribution of existing wealth would not make any significant difference to the people. Thus, a need for a dynamic national policy directed towards a continuous increase in production and productivity by all possible means, side by side with measures to secure its equal distribution was felt. The Government in this context adopted in 1948 an Industrial Policy Resolution, a historic document and a trend setter, which emphasised on importance to the economy of securing a continuous increase in the production and its equitable distribution and pointed out that state must play a progressively active role in the development of industries.

The resolution envisioned that besides arms, ammunition, atomic energy and railway transportation, to be the monopoly of the Central Government, the States would be exclusively responsible for the establishment of new undertakings in basic industries except where, in the national interest, the State itself found it necessary to secure the cooperation of the private enterprise. The rest of the industrial areas were thrown open to private enterprise, though it was made clear that the State would also progressively participate in this field.

Recognising the valuable role of private enterprise in the economy, the resolution emphasised that the States could contribute more quickly to the increase of national wealth by expanding its present activities where it is already operating and by concentrating on new units of production in other fields, rather than acquiring and running existing units. The resolution also recognized the importance of participation of foreign capital and enterprise, particularly in relation to industrial technology and knowledge, for the rapid industrialization of India. The Industrial Policy Resolution 1948 was provided legal support by enacting Industries (Development and Regulation) Act, 1951 and vesting in the Government necessary powers to regulate and control the existing and future undertakings.

Industrial Policy Resolution, 1956

The Industrial Policy Resolution of 1956 laid down the basic approach towards industrial development. The new policy thrust rightly recognised the Directive Principles of State Policy enshrined in the Constitution and the adoption by the Parliament in December 1954 of the socialist pattern of society as the objective of social and economic policy.

In order to realise the socialistic pattern of society, the Government recognised the need to accelerate the rate of economic growth and to speed up industrialization and, in particular, to develop heavy industries and machine making industries, to expand the public sector. The Government also felt the need to prevent private monopolies and the concentration of economic power in different fields in the hands of small number of individuals.

The Government classified industries into three categories. The first category included those industries the future development of which was the exclusive responsibility of States. The second category included progressively State owned industries and areas in which the States had to take initiatives to establish new undertakings, though the private participation was also expected to supplement the Government efforts. The third category included all the remaining industries with the responsibility of private sector for their development.

The Industrial Policy Resolution of 1956 was followed by the Industrial Policy Statement of 1973 which, *inter alia*, identified high priority industries for investment by large Industrial houses and foreign companies. Emphasis on de-centralisation and on the role of small scale, tiny and cottage industries was the hallmark of the Industrial Policy Statement of 1977. The Industrial Policy Statement of 1980 focussed attention on the need for promoting competition in the domestic market, technological upgradation and modernisation. The policy laid down the foundation for an increasingly competitive export base and for encouraging foreign investment in high technology areas. These policies created a climate for rapid industrial growth in our country. A number of policy and procedural changes were also introduced in the years 1985 and 1986 aimed at increasing productivity, reducing costs and improving quality.

New Industrial Policy, 1991

The statement on New Industrial Policy, 1991 was tabled in the Parliament on 24th July, 1991, at the time when the Government of India faced severest foreign exchange resource crunch. This document admitted candidly the policy distortions of the past and expressed the Government's earnestness to achieve a break through in its policy formulations.

The statement states that "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 Competition……" Pursuant to this, the Government initiated a series of measures in the areas of Industrial licensing, foreign investment, foreign technology agreements, public sector policy.

The Industrial Policy Resolution of 1956 and the statement on Industrial Policy of 1991 provide the basic framework for overall industrial policy of the Government. Over the years, adjustments have been made in the policy to accelerate the pace of industrial growth by providing greater freedom in investment decisions keeping in view the objectives of efficiency and competitiveness, technological upgradation, maximisation of capacity utilisation and increased growth.

The thrust of the New Industrial Policy of 1991 has, therefore, been to inject new dosage of competition in order to induce greater industrial efficiency and international competitiveness. The domestic competition has been induced by delicensing of industries and liberalising the policy related to foreign direct investment.

Since July 1991, the Indian industry has undergone a sea change in terms of the basic parameters governing its structure and functioning. The major reforms include large scale reduction in the scope of industrial incensing, simplification of procedural rules and regulations, reduction of areas reserved exclusively for the public sector,

disinvestment of equity in selected public sector undertakings, enhancing the limits of foreign equity participation in domestic industrial undertakings, liberalisation of trade and exchange rate policies, rationalisation and reduction of customs and excise duties and personal and corporate tax.

With a view to ensure efficient allocation of resources, banking and capital markets also came in for major economic reforms. The banking sector reforms included substantial interest rate deregulation, liberal incensing of private sector banks, and expansion of the branch network of foreign banks. The capital market reforms aimed at de-linking capital market from direct government controls, by a system of better disclosure, greater transparency and wider investor protection.

Separate policy measures were announced in the form of specific packages aimed at upliftment of the small scale, tiny and cottage industries as well as 100% Export Oriented Units, and units located in the Export Processing Zones and Technology Parks.

FDI POLICY FRAMEWORK IN INDIA

There has been a sea change in India's approach to foreign investment from the early 1990s when it began structural economic reforms encompassing almost all the sectors of the economy. Historically, India had followed an extremely cautious and selective approach while formulating FDI policy in view of the dominance of 'import-substitution strategy' of industrialisation. With the objective of becoming 'self reliant', there was a dual nature of policy intention – FDI through foreign collaboration was welcomed in the areas of high technology and high priorities to build national capability and discouraged in low technology areas to protect and nurture domestic industries. The regulatory framework was consolidated through the enactment of Foreign Exchange Regulation Act (FERA), 1973 wherein foreign equity holding in a joint venture was allowed only up to 40 per cent. Subsequently, various exemptions were extended to foreign companies engaged in export oriented businesses and high technology and high priority areas including allowing equity holdings of over 40 per cent. Moreover, drawing from successes of other country experiences in Asia, Government not only established special economic zones (SEZs) but also designed liberal policy and provided incentives for promoting FDI in these zones with a view to promote exports. As India continued to be highly protective, these measures did not add substantially to export competitiveness. Recognising these limitations, partial liberalisation in the trade and investment policy was introduced in the 1980s with the objective of enhancing export competitiveness, modernisation and marketing of exports through Trans-national Corporations (TNCs). The announcements of Industrial Policy (1980 and 1982) and Technology Policy (1983) provided for a liberal attitude towards foreign investments in terms of changes in policy directions. The policy was characterised by de-licensing of some of the industrial rules and promotion of Indian manufacturing exports as well as emphasising on modernisation of industries through liberalised imports of capital goods and technology. This was supported by trade liberalisation measures in the form of tariff reduction and shifting of large number of items from import licensing to Open General Licensing (OGL).

A major shift occurred when India embarked upon economic liberalisation and reforms program in 1991 aiming to raise its growth potential and integrating with the world economy. Industrial policy reforms gradually removed restrictions on investment projects and business expansion on the one hand and allowed increased access to foreign technology and funding on the other. A series of measures that were directed towards liberalizing foreign investment included:

(a) introduction of dual route of approval of FDI – RBI's automatic route and Government's approval (SIA/FIPB) route,

(b) automatic permission for technology agreements in high priority industries and removal of restriction of FDI in low technology areas as well as liberalisation of technology imports,

(c) permission to Non-resident Indians (NRIs) and Overseas Corporate Bodies (OCBs) to invest up to 100 per cent in high priorities sectors,

(d) hike in the foreign equity participation limits to 51 per cent for existing companies and liberalisation of the use of foreign 'brands name' and

(e) signing the Convention of Multilateral Investment Guarantee Agency (MIGA) for protection of foreign investments.

These efforts were boosted by the enactment of Foreign Exchange Management Act (FEMA), 1999 [that replaced the Foreign Exchange Regulation Act (FERA), 1973] which was less stringent. This along with the sequential financial sector reforms paved way for greater capital account liberalisation in India.

ROLE OF DEPARTMENT OF INDUSTRIAL POLICY & PROMOTION

The Department of Industrial Policy & Promotion is the nodal department for formulation of the policy of the Government on Foreign Direct Investment (FDI). It is also responsible for maintenance and management of data on inward FDI into India, based upon the remittances reported by the Reserve Bank of India.

DIPP plays an active role in the liberalization and rationalization of the FDI policy. Towards this end, it has been constructively engaged in extensive stakeholder consultations on various aspects of the FDI policy. The Department also plays an active role in investment promotion, through dissemination of information on the investment climate and opportunities in India and by advising prospective investors about investment policies, procedures and opportunities. International Cooperation for industrial partnerships is solicited through both-bilateral, as well as multilateral arrangements. It also coordinates with apex industry associations, in their activities relating to promotion of industrial cooperation, through both-bilateral, as well as multilateral initiatives intended to stimulate the inflow of foreign direct investment into India.

FDI POLICY OF INDIA

Foreign Direct Investment (FDI) is a category of cross border investment made by a resident in one economy (the direct investor) with the objective of establishing a 'lasting interest' in an enterprise (the direct investment enterprise) i.e. resident in an economy other than that of the direct investor. The motivation of the direct investor is a strategic long term relationship with the direct investment enterprise to ensure the significant degree of influence by the direct investor in the management of the direct investment enterprise. The objectives of direct investment are different from those of portfolio investment whereby investors do not generally expect to influence the management of the enterprise.

FDI-means investment, by a non-resident entity/person resident outside India in the capital of an Indian company, under Schedule 1 of the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000.

Foreign Direct Investment (FDI) in India is undertaken in accordance with the FDI Policy which is formulated and announced by the Government of India. The Department of Industrial Policy and Promotion, Ministry of Commerce and Industry, Government of India issues a "Consolidated FDI Policy Circular " on an yearly basis on March 31 of each year (since 2010) elaborating the policy and the process in respect of FDI in India. Latest Consolidated FDI policy was released with effect from 17th April 2014 with the intent and objective of the Government of India to attract and promote foreign direct investment in order to supplement domestic capital, technology and skills, for accelerated economic growth. It is governed by the provisions of the Foreign Exchange Management Act (FEMA), 1999.

Government has put in place a liberal policy on FDI, under which FDI, up to 100%, is permitted, under the automatic route, in most sectors/activities. There is a small list of sectors, which are either prohibited for FDI, or are subject to restrictions in the nature of equity caps, entry route or conditionalities. Further, the FDI policy is reviewed on an ongoing basis, with a view to making it more investor-friendly. Significant changes have been made in the FDI policy regime in recent times, to ensure that India remains an increasingly attractive investment destination.

Some of the basic provisions of Consolidated FDI policy of India are given below:

1. Forms in which business can be conducted by a foreign company in India:

A foreign company planning to set up business operations in India may:

- Incorporate a company under the Companies Act, 1956, as a Joint Venture or a Wholly Owned Subsidiary.
- Set up a Liaison Office / Representative Office or a Project Office or a Branch Office of the foreign company which can undertake activities permitted under the Foreign Exchange Management (Establishment in India of Branch Office or Other Place of Business) Regulations, 2000.

2. Procedure for receiving Foreign Direct Investment in an Indian company:

An Indian company may receive Foreign Direct Investment under the two routes as given under:

(i) Automatic Route: FDI is allowed under the automatic route without prior approval either of the Government or the Reserve Bank of India in all activities/sectors as specified in the consolidated FDI Policy, issued by the Government of India from time to time.

(**ii) Government Route:** FDI in activities not covered under the automatic route requires prior approval of the Government which are considered by the Foreign Investment Promotion Board (FIPB), Department of Economic Affairs, and Ministry of Finance. Application can be made in Form FC-IL, which can be downloaded from http://www.dipp.gov.in. Plain paper applications carrying all relevant details are also accepted. No fee is payable.

The Indian company having received FDI either under the **Automatic route** or the **Government route** is required to comply with provisions of the FDI policy including reporting the FDI to the Reserve Bank.

3. Instruments for receiving Foreign Direct Investment in an Indian company:

Foreign investment is reckoned as FDI only if the investment is made in equity shares, fully and mandatorily convertible preference shares and fully and mandatorily convertible debentures with the pricing being decided upfront as a figure or based on the formula that is decided upfront. Any foreign investment into an instrument issued by an Indian company which:

- gives an option to the investor to convert or not to convert it into equity or
- does not involve upfront pricing of the instrument

as a date would be reckoned as ECB and would have to comply with the ECB guidelines.

The FDI policy provides that the price/ conversion formula of convertible capital instruments should be determined upfront at the time of issue of the instruments. The price at the time of conversion should not in any case be lower than the fair value worked out, at the time of issuance of such instruments, in accordance with the extant FEMA regulations [the DCF method of valuation for the unlisted companies and valuation in terms of SEBI (ICDR) Regulations, for the listed companies].

4. Modes of payment allowed for receiving Foreign Direct Investment in an Indian company:

An Indian company issuing shares /convertible debentures under FDI Scheme to a person resident outside India shall receive the amount of consideration required to be paid for such shares /convertible debentures by:

(i) inward remittance through normal banking channels.

(ii) debit to NRE / FCNR account of a person concerned maintained with an AD category I bank.

(iii) conversion of royalty / lump sum / technical know how fee due for payment or conversion of ECB, shall be treated as consideration for issue of shares.

(iv) conversion of import payables / pre incorporation expenses / share swap can be treated as consideration for issue of shares with the approval of FIPB.

(v) debit to non-interest bearing Escrow account in Indian Rupees in India which is opened with the approval from AD Category – I bank and is maintained with the AD Category I bank on behalf of residents and non-residents towards payment of share purchase consideration.

If the shares or convertible debentures are not issued within 180 days from the date of receipt of the inward remittance or date of debit to NRE / FCNR (B) / Escrow account, the amount shall be refunded. Further, Reserve Bank may on an application made to it and for sufficient reasons permit an Indian Company to refund / allot shares for the amount of consideration received towards issue of security if such amount is outstanding beyond the period of 180 days from the date of receipt.

5. Sectors where FDI is not allowed in India, both under the Automatic Route as well as under the Government Route:

FDI is prohibited under the Government Route as well as the Automatic Route in the following sectors:

(i) Atomic Energy

(ii) Lottery Business

(iii) Gambling and Betting

(iv) Business of Chit Fund

(v) Nidhi Company

(vi) Agricultural (excluding Floriculture, Horticulture, Development of seeds, Animal Husbandry, Pisciculture and cultivation of vegetables, mushrooms, etc. under controlled conditions and services related to agro and allied sectors) and Plantations activities (other than Tea Plantations) (c.f. Notification No. FEMA 94/ 2003-RB dated June 18, 2003).

(vii) Housing and Real Estate business (except development of townships, construction of residen-tial/ commercial premises, roads or bridges to the extent specified in Notification No. FEMA 136/2005-RB dated July 19, 2005).

(viii) Trading in Transferable Development Rights (TDRs).

(ix) Manufacture of cigars, cheroots, cigarillos and cigarettes, of tobacco or of tobacco substitutes.

Note : Student can also see the website of Department of Industrial Policy and Promotion (DIPP), Ministry of Commerce & Industry, Government of India at www.dipp.gov.in for details regarding sectors and investment limits therein allowed, under FDI. A Table is given at the end of this topic summarising sector specific limits.

6. Procedure to be followed after investment is made under the Automatic Route or with Government approval:

A two-stage reporting procedure has to be followed:

(i) On receipt of share application money:

Within 30 days of receipt of share application money/amount of consideration from the non-resident investor, the Indian company is required to report to the Foreign Exchange Department, Regional Office concerned of the Reserve Bank of India, under whose jurisdiction its Registered Office is located, the Advance Reporting Form, containing the following details :

– Name and address of the foreign investor/s;

– Date of receipt of funds and the Rupee equivalent;

– Name and address of the authorised dealer through whom the funds have been received;

– Details of the Government approval, if any; and

– KYC report on the non-resident investor from the overseas bank remitting the amount of consideration.

The Indian company has to ensure that the shares are issued within 180 days from the date of inward remittance which otherwise would result in the contravention / violation of the FEMA regulations.

(ii) Upon issue of shares to non-resident investors:

Within 30 days from the date of issue of shares, a report in Form FC-GPR- PART A together with the following documents should be filed with the Foreign Exchange Department, Regional Office concerned of the Reserve Bank of India.

– Certificate from the Company Secretary of the company accepting investment from persons resident outside India certifying that: The company has complied with the procedure for issue of shares as laid down under the FDI scheme as indicated in the Notification No. FEMA 20/2000-RB dated 3rd May 2000, as amended from time to time.

– The investment is within the sectoral cap / statutory ceiling permissible under the Automatic Route of the Reserve Bank and it fulfills all the conditions laid down for investments under the Automatic Route,

– **OR**

– Shares have been issued in terms of SIA/FIPB approval No. ———————— dated ———— ———————— (enclosing the FIPB approval copy)

– Certificate from Statutory Auditors/ SEBI registered Merchant Banker / Chartered Accountant indicating the manner of arriving at the price of the shares issued to the persons resident outside India.

7. Guidelines for transfer of existing shares from non-residents to residents or residents to non-residents:

The term 'transfer' is defined under FEMA as including "sale, purchase, acquisition, mortgage, pledge, gift, loan or any other form of transfer of right, possession or lien" {Section 2 (ze) of FEMA, 1999}.

The following share transfers are allowed without the prior approval of the Reserve Bank of India

A. Transfer of shares from a Non Resident to Resident under the FDI scheme where the pricing guidelines under FEMA, 1999 are not met provided that :-

(i) The original and resultant investment are in line with the extant FDI policy and FEMA regulations in terms of sectoral caps, conditionalities (such as minimum capitalization, etc.), reporting requirements, documentation, etc.;

(ii) The pricing for the transaction is compliant with the specific/explicit, extant and relevant SEBI regulations / guidelines (such as IPO, Book building, block deals, delisting, exit, open offer/ substantial acquisition / SEBI SAST, buy back); and

(iii) Chartered Accountants Certificate to the effect that compliance with the relevant SEBI regulations / guidelines as indicated above is attached to the form FC-TRS to be filed with the AD bank.

B. Transfer of shares from Resident to Non Resident:

(i) where the transfer of shares requires the prior approval of the FIPB as per the extant FDI policy provided that :

– the requisite approval of the FIPB has been obtained; and

- the transfer of share adheres with the pricing guidelines and documentation requirements as specified by the Reserve Bank of India from time to time.

(ii) where SEBI (SAST) guidelines are attracted subject to the adherence with the pricing guidelines and documentation requirements as specified by Reserve Bank of India from time to time.

(**iii) where the pricing guidelines under the Foreign Exchange Management Act (FEMA), 1999 are not met provided that:-** The resultant FDI is in compliance with the extant FDI policy and FEMA regulations in terms of sectoral caps, conditionalities (such as minimum capitalization, etc.), reporting requirements, documentation etc.; b) The pricing for the transaction is compliant with the specific/explicit, extant and relevant SEBI regulations / guidelines (such as IPO, Book building, block deals, delisting, exit, open offer/ substantial acquisition / SEBI SAST); and Chartered Accountants Certificate to the effect that compliance with the relevant SEBI regulations / guidelines as indicated above is attached to the form FC-TRS to be filed with the AD bank.

(iv) where the investee company is in the financial sector provided that :

- NOCs are obtained from the respective financial sector regulators/ regulators of the investee company as well as transferor and transferee entities and such NOCs are filed along with the form FC-TRS with the AD bank; and
- The FDI policy and FEMA regulations in terms of sectoral caps, conditionalities (such as minimum capitalization, etc.), reporting requirements, documentation etc., are complied with.

Where non-residents (including NRIs) make investment in an Indian company in compliance with the provisions of the Companies Act, 1956, by way of subscription to Memorandum of Association, such investments may be made at face value subject to their eligibility to invest under the FDI scheme.

C. Transfer of shares/ fully and mandatorily convertible debentures by way of Gift:

A person resident outside India can freely transfer shares/ fully and mandatorily convertible debentures by way of gift to a person resident in India as under:

- Any person resident outside India, (not being a NRI or an erstwhile OCB), can transfer by way of gift the shares/ fully and mandatorily convertible debentures to any person resident outside India;
- a NRI may transfer by way of gift, the shares/convertible debentures held by him to another NRI only,
- Any person resident outside India may transfer share/ fully and mandatorily convertible debentures to a person resident in India by way of gift.

8. Transfer of security by way of gift to a person resident outside India by a person resident in India:

A person resident in India who proposes to transfer security **by way of gift** to a person resident outside India [other than erstwhile OCBs] shall make an application to the Central Office of the Foreign Exchange Department, Reserve Bank of India furnishing the following information, namely:

- Name and address of the transferor and the proposed transferee
- Relationship between the transferor and the proposed transferee
- Reasons for making the gift.
- In case of Government dated securities, treasury bills and bonds, a certificate issued by a Chartered Accountant on the market value of such securities.
- In case of units of domestic mutual funds and units of Money Market Mutual Funds, a certificate from the issuer on the Net Asset Value of such security.

- In case of shares/ fully and mandatorily convertible debentures, a certificate from a Chartered Account on the value of such securities according to the guidelines issued by the Securities & Exchange Board of India or the Discount Free Cash Flow Cash (DCF) method with regard to listed companies and unlisted companies, respectively.
- Certificate from the Indian company concerned certifying that the proposed transfer of shares/convertible debentures, by way of gift, from resident to the non-resident shall not breach the applicable sectoral cap/ FDI limit in the company and that the proposed number of shares/convertible debentures to be held by the non-resident transferee shall not exceed 5 per cent of the paid up capital of the company.

The transfer of security by way of gift may be permitted by the Reserve bank provided:

(i) The donee is eligible to hold such security under Schedules 1, 4 and 5 to Notification No. FEMA 20/ 2000-RB dated May 3, 2000, as amended from time to time.

(ii) The gift does not exceed 5 per cent of the paid up capital of the Indian company/ each series of debentures/ each mutual fund scheme

(iii) The applicable sectoral cap/ foreign direct investment limit in the Indian company is not breached

(iv) The donor and the donee are relatives as defined in section 6 of the Companies Act, 1956.

(v) The value of security to be transferred by the donor together with any security transferred to any person residing outside India as gift in the financial year does not exceed the rupee equivalent of USD 50000.

(vi) Such other conditions as considered necessary in public interest by the Reserve Bank.

9. Transfer of shares from resident to non-resident under the following categories:

(a) Transfer of Shares by Resident which requires Government approval

The following instances of transfer of shares from residents to non-residents by way of sale or otherwise requires Government approval:

(i) Transfer of shares of companies engaged in sector falling under the Government Route.

(ii) Transfer of shares resulting in foreign investments in the Indian company, breaching the sectoral cap applicable.

(b) Prior permission of the Reserve Bank in certain cases for acquisition / transfer of security

(i) Transfer of shares or convertible debentures from residents to non-residents by way of sale requires prior approval of Reserve Bank in case where the non-resident acquirer proposes deferment of payment of the amount of consideration. Further, in case approval is granted for the transaction, the same should be reported in Form FC-TRS to the AD Category – I bank, within 60 days from the date of receipt of the full and final amount of consideration.

(ii) A person resident in India, who intends to transfer any security, by way of gift to a person resident outside India, has to obtain prior approval from the Reserve Bank.

(c) Any other case not covered by General Permission.

10. Reporting obligations in case of transfer of shares between resident and non-resident:

The transaction should be reported by submission of form FC-TRS to the AD Category – I bank, within 60 days from the date of receipt/remittance of the amount of consideration. The onus of submission of the form FC-TRS within the given timeframe would be on the resident in India, the transferor or transferee, as the case may be.

11. Method of payment and remittance/credit of sale proceeds in case of transfer of shares between resident and non-resident:

The sale consideration in respect of the shares purchased by a person resident outside India shall be remitted to India through normal banking channels. In case the buyer is a Foreign Institutional Investor (FII), payment should be made by debit to its Special Non-Resident Rupee Account. In case the buyer is a NRI, the payment may be made by way of debit to his NRE/FCNR (B) accounts. However, if the shares are acquired on non-repatriation basis by NRI, the consideration shall be remitted to India through normal banking channel or paid out of funds held in NRE/FCNR (B)/NRO accounts.

The sale proceeds of shares (net of taxes) sold by a person resident outside India) may be remitted outside India. In case of FII the sale proceeds may be credited to its special Non-Resident Rupee Account. In case of NRI, if the shares sold were held on repatriation basis, the sale proceeds (net of taxes) may be credited to his NRE/FCNR(B) accounts and if the shares sold were held on non repatriation basis, the sale proceeds may be credited to his NRO account subject to payment of taxes. The sale proceeds of shares (net of taxes) sold by an erstwhile OCB may be remitted outside India directly if the shares were held on repatriation basis and if the shares sold were held on non-repatriation basis, the sale proceeds may be credited to its NRO (Current) Account subject to payment of taxes, except in the case of erstwhile OCBs whose accounts have been blocked by Reserve Bank.

12. Investments and profits earned in India repatriable or not:

All foreign investments are freely repatriable (net of applicable taxes) except in cases where:

(i) the foreign investment is in a sector like Construction and Development Projects and Defence wherein the foreign investment is subject to a lock-in-period; and

(ii) NRIs choose to invest specifically under non-repatriable schemes.

Further, dividends (net of applicable taxes) declared on foreign investments can be remitted freely through an Authorised Dealer bank.

13. Guidelines on issue and valuation of shares in case of existing companies:

A. The price of shares issued to persons resident outside India under the FDI Scheme shall not be less than:

(i) the price worked out in accordance with the SEBI guidelines, as applicable, where the shares of the company is listed on any recognised stock exchange in India;

(ii) the fair valuation of shares done by a SEBI registered Category - I Merchant Banker or a Chartered Accountant as per the discounted free cash flow method, where the shares of the company is not listed on any recognised stock exchange in India; and

(iii) the price as applicable to transfer of shares from resident to non-resident as per the pricing guidelines laid down by the Reserve Bank from time to time, where the issue of shares is on preferential allotment.

B. The price of shares transferred from resident to a non-resident and vice versa should be determined as under:

(i) Transfer of shares from a resident to a non-resident:

(a) In case of listed shares, at a price which is not less than the price at which a preferential allotment of shares would be made under SEBI guidelines.

(b) In case of unlisted shares at a price which is not less than the fair value as per the Discount Free Cash Flow (DCF) Method to be determined by a SEBI registered Category-I- Merchant Banker/ Chartered Accountant.

(ii) Transfer of shares from a non-resident to a resident - The price should not be more than the minimum price at which the transfer of shares would have been made from a resident to a non-resident.

In any case, the price per share arrived at as per the above method should be certified by a SEBI registered Category-I-Merchant Banker / Chartered Accountant.

14. Regulations pertaining to issue of ADRs/ GDRs by Indian companies:

- Indian companies can raise foreign currency resources abroad through the issue of ADRs/ GDRs, in accordance with the Scheme for issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993 and guidelines issued by the Government of India thereunder from time to time.
- A company can issue ADRs / GDRs, if it is eligible to issue shares to persons resident outside India under the FDI Scheme. However, an Indian listed company, which is not eligible to raise funds from the Indian Capital Market including a company which has been restrained from accessing the securities market by the Securities and Exchange Board of India (SEBI) will not be eligible to issue ADRs/ GDRs.
- Unlisted companies, which have not yet accessed the ADR/GDR route for raising capital in the international market, would require prior or simultaneous listing in the domestic market, while seeking to issue such overseas instruments. Unlisted companies, which have already issued ADRs/GDRs in the international market, have to list in the domestic market on making profit or within three years of such issue of ADRs/GDRs, whichever is earlier.
- After the issue of ADRs/GDRs, the company has to file a return in Form DR as indicated in the RBI Notification No. FEMA.20/ 2000-RB dated May 3, 2000, as amended from time to time. The company is also required to file a quarterly return in Form DR- Quarterly as indicated in the RBI Notification ibid.
- There are no end-use restrictions on GDR/ADR issue proceeds, except for an express ban on investment in real estate and stock markets.
- Erstwhile OCBs which are not eligible to invest in India and entities prohibited to buy, sell or deal in securities by SEBI will not be eligible to subscribe to ADRs / GDRs issued by Indian companies.
- The pricing of ADR / GDR issues including sponsored ADRs / GDRs should be made at a price determined under the provisions of the Scheme of issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993 and guidelines issued by the Government of India and directions issued by the Reserve Bank, from time to time.

15. Sponsored ADR & Two-way fungibility Scheme of ADR / GDR:

Sponsored ADR/GDR: An Indian company may sponsor an issue of ADR/ GDR with an overseas depository against shares held by its shareholders at a price to be determined by the Lead Manager. The operative guidelines for the same have been issued vide A.P. (DIR Series) Circular No.52 dated November 23, 2002.

Two-way fungibility Scheme: Under the limited Two-way fungibility Scheme, a registered broker in India can purchase shares of an Indian company on behalf of a person resident outside India for the purpose of converting the shares so purchased into ADRs/ GDRs. The operative guidelines for the same have been issued vide A.P. (DIR Series) Circular No.21 dated February 13, 2002. The Scheme provides for purchase and re-conversion of only as many shares into ADRs/ GDRs which are equal to or less than the number of shares emerging on surrender of ADRs/ GDRs which have been actually sold in the market. Thus, it is only a limited two-way fungibility wherein the headroom available for fresh purchase of shares from domestic market is restricted to the number of converted shares sold in the domestic market by non-resident investors. So long the ADRs/ GDRs are quoted at discount to the value of shares in domestic market, an investor will gain by converting the ADRs/ GDRs into underlying shares and selling them in the domestic market. In case of ADRs/ GDRs being quoted at premium, there will be demand for reverse fungibility, i.e. purchase of shares in domestic market for re-conversion

into ADRs/ GDRs. The scheme is operationalised through the Custodians of securities and stock brokers under SEBI.

16. Foreign Currency Convertible Bonds (FCCBs):

FCCBs can be issued by Indian companies in the overseas market in accordance with the Scheme for Issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993.

The FCCB being a debt security, the issue needs to conform to the External Commercial Borrowing guidelines, issued by RBI vide Notification No. FEMA 3/2000-RB dated May 3, 2000, as amended from time to time.

17. Investment in Preference Shares by foreign investor:

Yes. Foreign investment through preference shares is treated as foreign direct investment. However, the preference shares should be fully and mandatorily convertible into equity shares within a specified time to be reckoned as part of share capital under FDI. Investment in other forms of preference shares requires to comply with the ECB norms.

18. Debentures as part of FDI:

Yes. Debentures which are fully and mandatorily convertible into equity within a specified time would be reckoned as part of share capital under the FDI Policy.

19. Issue of shares against Lumpsum Fee, Royalty, ECB , Import of capital goods/ machineries / equipments (excluding second-hand machine) and Pre-operative/pre-incorporation expenses (including payments of rent):

An Indian company eligible to issue shares under the FDI policy and subject to pricing guidelines as specified by the Reserve Bank from time to time, may issue shares to a person resident outside India :

(i) being a provider of technology / technical know-how, against Royalty / Lumpsum fees due for payment;

(ii) against External Commercial Borrowing (ECB) (other than import dues deemed as ECB or Trade Credit as per RBI Guidelines).

(iii) With prior approval from FIPB for against import of capital goods/ machineries / equipments and Pre-operative/pre-incorporation expenses subject to the compliance with the extant FEMA regulations and AP Dir Series 74 dated June 30,2011.

Provided, that the foreign equity in the company, after such conversion, is within the sectoral cap.

20. Other modes of issues of shares for which general permission is available under RBI Notification No. FEMA 20 dated May 3, 2000:

– Issue of shares under ESOP by Indian companies to its employees or employees of its joint venture or wholly owned subsidiary abroad who are resident outside India directly or through a Trust up to 5% of the paid up capital of the company.

– Issue and acquisition of shares by non-residents after merger or de-merger or amalgamation of Indian companies.

– Issue shares or preference shares or convertible debentures on rights basis by an Indian company to a person resident outside India.

21. Investment in shares issued by an unlisted company in India:

Yes. As per the regulations/guidelines issued by the Reserve Bank of India/Government of India, investment can be made in shares issued by an unlisted Indian company.

22. Setting up a partnership/ proprietorship concern in India by foreigner:

No. Only NRIs/PIOs are allowed to set up partnership/proprietorship concerns in India **on non-repatriation basis**.

23. Investment in Rights shares issued by an Indian company at a discount:

There are no restrictions under FEMA for investment in Rights shares issued at a discount by an Indian company, provided the rights shares so issued are being offered at the same price to residents and non-residents. The offer on right basis to the person's resident outside India shall be:

(i) in the case of shares of a company listed on a recognized stock exchange in India, at a price as determined by the company; and

(ii) in the case of shares of a company not listed on a recognized stock exchange in India, at a price which is not less than the price at which the offer on right basis is made to resident shareholders.

24. Pledging of shares AD bank allow pledge of shares of an Indian company held by non-resident investor in favor of an Indian bank or an Overseas bank vide the instruction and subject to compliance with the terms and conditions as mentioned in the AP Dir Series Circular No 57 dated May 2, 2011.

Current FDI policy in terms of sector specific limits has been summarised in Table below:

Table: Sector Specific Limits of Foreign Investment in India

Sl. No.	Sector/Activity Equity	% of FDI Cap/	Entry Route
1	**AGRICULTURE & ANIMAL HUSBANDRY** (a) Floriculture, Horticulture, Apiculture and Cultivation of Vegetables & Mushrooms under controlled conditions; (b) Development and production of Seeds and planting material; (c) Animal Husbandry (including breeding of dogs), Pisciculture, Aquaculture, under controlled conditions; and (d) Services related to agro and allied sectors *Note: Besides the above, FDI is not allowed in any other agricultural sector/activity*	100%	Automatic
2	**TEA PLANTATION** Tea sector including tea plantations *Note: Besides the above, FDI is not allowed in any other plantation sector/activity*	100%	Government
3	**MINING**		
	Mining and Exploration of metal and non-metal ores including diamond, gold, silver and precious ores but excluding titanium bearing minerals and its ores; **subject to** the Mines and Minerals (Development & Regulation) Act, 1957.	100%	Automatic
	Coal & Lignite mining for captive consumption by power projects, iron & steel and cement units and other eligible activities and Setting up coal processing plants like washeries **subject to certain** condition.	100%	Automatic
	Mining and mineral separation of titanium bearing minerals & ores,	100%	Government

	its value addition and integrated activities.		
4	**PETROLEUM & NATURAL GAS** Exploration activities of oil and natural gas fields, infrastructure related to marketing of petroleum products and natural gas, marketing of natural gas and petroleum products, petroleum product pipelines, natural gas/ pipelines, LNG Regasification infrastructure, market study and formulation and Petroleum refining in the private sector, **subject to** the existing sectoral policies.	100%	Automatic
	Petroleum refining by the Public Sector Undertakings (PSU), without any disinvestment or dilution of domestic equity in the existing PSUs.	49%	Government
5	**MANUFACTURING** **Manufacture of items reserved for production in Micro and Small Enterprises (MSEs)** will be subject to the sectoral caps, entry routes and other relevant sectoral regulations.		
	Any industrial undertaking which is not a MSE, but manufactures items reserved for the MSE sector subject to certain conditions.	100%	Automatic Upto 24% More than 24% Government route
6	**DEFENCE** Defence Industry subject to Industrial license under the Industries (Development & Regulation) Act 1951.	26%	Government
7	**BROADCASTING SERVICES**		
	(a) Broadcasting Carriage Services (1) **Teleports** (setting up of up-linking HUBs/Teleports); (2) **Direct to Home** (DTH); (3) **Cable Networks** (Multi System operators (MSOs) operating at National or State or District level and undertaking upgradation of networks towards digitalization and addressability); (4) **Mobile TV;** (5) **Headend-in-the Sky Broadcasting Service** (HITS)	74%	Automatic up to 49% Government route beyond 49% and up
	Cable Networks (Other MSOs not undertaking upgradation of networks towards digitalization and addressability and Local Cable Operators (LCOs)	49%	Automatic
	(b) Broadcasting Content Services		
	Terrestrial Broadcasting FM (FM Radio), subject to such terms and conditions, as specified from time to time, by Ministry of Information & Broadcasting, for grant of permission for setting up of FM Radio stations.	26%	Government
	Up-linking of 'News & Current Affairs' TV Channels	26%	Government
	Up-linking of Non-'News & Current Affairs' TV Channels/ Down-linking of TV Channels	100%	Government

8	**PRINT MEDIA**		
	Publishing of Newspaper and periodicals dealing with news and current affairs.	26% (FDI and investment by NRIs/PIOs/FII)	Government
	Publication of Indian editions of foreign magazines dealing with news and current affairs.	26% (FDI and investment by NRIs/ PIOs/FII)	Government
	Publishing/printing of Scientific and Technical Magazines/specialty journals/ periodicals, **subject to** compliance with the legal framework as applicable and guidelines issued in this regard from time to time by Ministry of Information and Broadcasting.	100%	Government
	Publication of facsimile edition of foreign newspapers.	100%	Government
9	**CIVIL AVIATION**		
(a)	**Airports**		
	(a) Greenfield projects	100%	Automatic
	(b) Existing projects	100%	Automatic up to 74% Government route beyond 74%
(b)	**Air Transport Services**		
	(1) Scheduled Air Transport Service/ Domestic Scheduled Passenger Airline	49% FDI (100% for NRIs)	Automatic
	(2) Non-Scheduled Air Transport Service	74% FDI (100% for NRIs)	Automatic up to 49% Government route beyond 49% and up to 74%
	(3) Helicopter services/seaplane services requiring DGCA approval	100%	Automatic
(c)	**Other services under Civil Aviation sector**		
	(1) Ground Handling Services **subject to** sectoral regulations and security clearance	74% FDI (100% for NRIs)	Automatic up to 49% Government route beyond 49% and up to 74%
	(2) Maintenance and Repair organizations; flying training institutes; and technical training institutions	100%	Automatic

10	**COURIER SERVICES for carrying packages, parcels and other items which do not come within the ambit of the Indian Post Office Act, 1898 and excluding the activity relating to the distribution of letters.**	100%	Government
11	**CONSTRUCTION DEVELOPMENT: Townships, Housing, Built-up infrastructure**		
	Townships, housing, built-up infrastructure and construction-development projects (which would include, but not be restricted to, housing, commercial premises, hotels, resorts, hospitals, educational institutions, recreational facilities, city and regional level infrastructure)	100%	Automatic
12	**INDUSTRIAL PARKS – new and existing**	**100%**	**Automatic**
13	**SATELLITES – Establishment and operation**, subject to the sectoral guidelines of Department of Space/ISRO	74%	Government
14 **15**	**PRIVATE SECURITY AGENCIES** **TELECOM SERVICES**	49%	Government
	Telecom services	74%	Automatic up to 49% Government route beyond 49%
	(a) Internet Service Providers with gateways (b) ISP s not providing gateways i.e. without gate-ways (both for satellite and marine cables)	74%	Automatic up to 49% Government route beyond 49% and up to 74%
	(a) Infrastructure provider providing dark fibre, right of way, duct space, lower (IP Category I) (b) Electronic Mail (c) Voice Mail	100%	Automatic up to 49% Government route beyond 49%
16	**TRADING**		
	Cash & Carry Wholesale Trading/ Wholesale Trading (including sourcing from MSEs)	100%	Automatic
	E-commerce activities	100%	Automatic
	Test marketing of such items for which a company has approval for manufacture, provided such test marketing facility will be for a period of two years, and investment in setting up manufacturing facility commences simultaneously with test marketing.	100%	Government
	Single Brand product retail trading	100%	Government
	Multi Brand Retail Trading	51%	Government

17	**FINANCIAL SERVICES SECTOR**		
(a)	**Asset Reconstruction Companies**	100% of paid-up capital of ARC (FDI+FII)	Automatic up to 49% Government route beyond 49%
(b)	**Banking –Private sector**	74% including investment by FIIs	Automatic up to 49% Government route beyond 49% and up to 74%
(c)	**Banking- Public Sector subject to** Banking Companies (Acquisition & Transfer of Undertakings) Acts 1970/80.	20% (FDI and Portfolio Investment)	Government
(d)	**Commodity Exchange**	49% (FDI & FII) [Investment by Registered FII under Portfolio Investment Scheme (PIS) will be limited to 23% and Investment under FDI Scheme limited to 26%]	Automatic
(e)	Credit Information Companies	74% (FDI & FII)	Automatic
(f)	Infrastructure companies in Securities Markets, namely, stock exchanges, depositories and clearing corporations, in compliance with SEBI Regulations	49% (FDI & FII) [FDI limit of 26 per cent and an FII limit of 23 per cent of the paid-up capital]	Automatic
(g)	Insurance	26%	Automatic
(h)	Foreign investment in NBFC is allowed under the automatic route in only the following activities:	100%	Automatic
	(i) Merchant Banking (ii) Under Writing (iii) Portfolio Management Services (iv) Investment Advisory Services (v) Financial Consultancy (vi) Stock Broking		

	(vii) Asset Management (viii) Venture Capital (ix) Custodian Services (x) Factoring (xi) Credit Rating Agencies (xii) Leasing & Finance (xiii) Housing Finance (xiv) Forex Broking (xv) Credit Card Business (xvi) Money Changing Business (xvii) Micro Credit (xviii) Rural Credit		
18	**PHARMACEUTICALS**		
	Greenfield	100%	Automatic
	Brownfield	100%	Government
19	**POWER EXCHANGES** registered under the Central Electricity Regulatory Commission (Power Market) Regulations, 2010	49% (FDI &FII)	Automatic
20	**FDI IS PROHIBITED IN:**		
	(a) Lottery Business including Government /private lottery, online lotteries, etc. (b) Gambling and Betting including casinos etc. (c) Chit funds (d) Nidhi company (e) Trading in Transferable Development Rights (TDRs) (f) Real Estate Business or Construction of Farm Houses (g) Manufacturing of Cigars, cheroots, cigarillos and cigarettes, of tobacco or of tobacco substitutes (h) Activities / sectors not open to private sector investment e.g. Atomic Energy and Railway Transport (other than Mass Rapid Transport Systems). **Foreign technology collaboration in any form** including licensing for franchise, trademark, brand name, management contract is also prohibited for Lottery Business and Gambling and Betting activities.		

FOREIGN INVESTMENT IMPLEMENTATION AUTHORITY (FIIA)

The Government has set up the Foreign Investment Implementation Authority (FIIA) in the Department of Industrial Policy & Promotion. The FIIA has been set up to facilitate expeditious implementation of Foreign Direct Investment (FDI) approvals; provide a pro-active one stop after case service to foreign investors by helping them obtain

necessary approvals, sort out operational problems and meet with various Government agencies to find solutions to problems.

Role: The role of the FIIA shall be to:

- understand and address concerns of investors;
- understand and address concerns of approving authorities;
- initiate multi agency consultations;
- refer matters not resolved at the FIIA level to higher levels on a quarterly basis, including cases of projects slippage on account of implementation bottlenecks.

Functions: The functions of the FIIA shall be as under:

- expediting various approvals / permissions;
- fostering partnership between investors and government agencies concerned;
- resolving difference in perceptions;
- enhancing overall credibility;
- reviewing the policy framework;
- liaising with the Ministry of External Affairs for keeping India-s diplomatic missions abroad informed about translation of FDI approvals into actual investment and implementation.

Constitution

(i) Secretary, D/o Industrial Chairman Policy and Promotion, Ministry of Commerce & Industry

(ii) Finance Secretary Member

(iii) Commerce Secretary Member

(iv) Secretary (Economic Member Relations), Ministry of External Affairs

(v) Secretary of the Member Administrative Ministry (to whom the proposal relates)

(vi) Chief Secretary of the State Member Government (to whom the proposal relates)

The FIIA may co-opt other Secretaries to the Government of India, Chief Commissioner (NRI), top functionaries of financial institutions and professional experts from industry and commerce, as and when necessary.

CASE STUDY ON FDI POLICY: THE INTERNATIONAL EXPERIENCE

Foreign direct investment is treated as an important mechanism for channelizing transfer of capital and technology and thus perceived to be a potent factor in promoting economic growth in the host countries. Moreover, multinational corporations consider FDI as an important means to reorganise their production activities across borders in accordance with their corporate strategies and the competitive advantage of host countries. These considerations have been the key motivating elements in the evolution and attitude of External Market Economics ('EMEs') towards investment flows from abroad in the past few decades particularly since the eighties. The following section reviews the FDI policies of some select Countries.

China

- Encouragement to FDI has been an integral part of the China's economic reform process. It has gradually opened up its economy for foreign businesses and has attracted large amount of direct foreign investment.

- Government policies were characterised by setting new regulations to permit joint ventures using foreign capital and setting up Special Economic Zones (SEZs) and Open Cities.The concept of SEZs was extended to fourteen more coastal cities in 1984.Favorable regulations and provisions were used to encourage FDI inflow, especially export-oriented joint ventures and joint ventures using advanced technologies in 1986.
- Foreign joint ventures were provided with preferential tax treatment, the freedom to import inputs such as materials and equipment, the right to retain and swap foreign exchange with each other, and simpler licensing procedures in 1986. Additional tax benefits were offered to export-oriented joint ventures and those employing advanced technology.
- Priority was given to FDI in the agriculture, energy, transportation, telecommunications, basic raw materials, and high-technology industries, and FDI projects which could take advantage of the rich natural resources and relatively low labour costs in the central and northwest regions.
- China's policies toward FDI have experienced roughly three stages: gradual and limited opening, active promoting through preferential treatment, and promoting FDI in accordance with domestic industrial objectives. These changes in policy priorities inevitably affected the pattern of FDI inflows in China.

Chile

- In Chile, policy framework for foreign investment, embodied in the constitution and in the Foreign Investment Statute, is quite stable and transparent and has been the most important factor in facilitating foreign direct investment. Under this framework, an investor signs a legal contract with the state for the implementation of an individual project and in return receives a number of specific guarantees and rights.
- Foreign investors in Chile can own up to 100 per cent of a Chilean based company, and there is no time limit on property rights. They also have access to all productive activities and sectors of the economy, except for a few restrictions in areas that include coastal trade, air transport and the mass media.
- Chile attracted investment in mining, services, electricity, gas and water industries and manufacturing.
- Investors are guaranteed the right to repatriate capital one year after its entry and to remit profits at any time.
- Although Chile's constitution is based on the principle of non-discrimination, some tax advantages are extended to foreign investors such as invariability of income tax regime, invariability of indirect taxes, and special policy regime for large projects.

Malaysia

- The Malaysian FDI regime is tightly regulated in that all foreign manufacturing activity must be licensed regardless of the nature of their business.
- Until 1998, foreign equity share limits were made conditional on performance and conditions set forth by the industrial policy of the time.
- In the past, the size of foreign equity share allowed for investment in the manufacturing sector hinged on the share of the products exported in order to support the country's export-oriented industrial policy.
- FDI projects that export at least 80 per cent of production or production involving advanced technology are promoted by the state and no equity conditions are imposed. Following the crisis in 1997-98, the restriction was abolished as the country was in need of FDI.

Korea

- The Korean government maintained distinctive foreign investment policies giving preference to loans over direct investment to supplement its low level of domestic savings during the early stage of industrialisation. Korea's heavy reliance on foreign borrowing to finance its investment requirements is in sharp contrast to other countries.
- The Korean Government had emphasised the need to enhance absorptive capacity as well as the indigenisation of foreign technology through **reverse engineering** at the outset of industrialisation while restricting both FDI and foreign licensing. This facilitated Korean firms to assimilate imported technology, which eventually led to emergence of global brands like Samsung, Hyundai, and LG.
- The Korean government pursued liberalised FDI policy regime in the aftermath of the Asian financial crisis in 1997-98 to fulfil the conditionality of the International Monetary Fund (IMF) in exchange for standby credit.
- Several new institutions came into being in Korea immediately after the crisis. Invest Korea is Korea's national investment promotion agency mandated to offer one-stop service as a means of attracting foreign direct investment, while the Office of the Investment Ombudsman was established to provide investment after-care services to foreign-invested companies in Korea. These are affiliated to the Korea Trade Investment Promotion Agency.
- Korea enacted a new foreign investment promotion act in 1998 to provide foreign investors incentives which include tax exemptions and reductions, financial support for employment and training, cash grants for R&D projects, and exemptions or reductions of leasing costs for land for factory and business operations for a specified period.
- One of the central reasons for the delays in the construction process in Korea is said to be the lengthy environmental and cultural due diligence on proposed industrial park sites. (OECD, 2008).

Thailand

- Thailand followed a traditional import-substitution strategy, imposing tariffs on imports, particularly on finished products in the 1960s. The role of state enterprises was greatly reduced from the 1950s and investment in infrastructure was raised. Attention was given to nurturing the institutional system necessary for industrial development. Major policy shift towards export promotion took place by early 1970s due to balance of payments problems since most of components, raw materials, and machinery to support the production process, had to be imported.
- On the FDI front, in 1977 a new Investment Promotion Law was passed which provided the Board of Investment (BOI) with more power to provide incentives to priority areas and remove obstacles faced by private investors (Table 4). After the East Asian financial crisis, the Thai government has taken a very favourable approach towards FDI with a number of initiatives to develop the industrial base and exports and progressive liberalisation of laws and regulations constraining foreign ownership in specified economic activities.
- The Alien Business Law, which was enacted in 1972 and restricted majority foreign ownership in certain activities, was amended in 1999. The new law relaxed limits on foreign participation in several professions such as law, accounting, advertising and most types of construction, which have been moved from a completely prohibited list to the less restrictive list of businesses.

To sum up, the spectacular performance of China in attracting large amount of FDI could be attributed to its proactive FDI policy comprising setting up of SEZs particularly exports catering to the international market, focus on infrastructure and comparative advantage owing to the low labour costs. A comparison of the FDI

policies pursued by select emerging economies, set out above, suggests that policies although broadly common in terms of objective, regulatory framework and focus on technological upgradation and export promotion, the use of incentive structure and restrictions on certain sectors, has varied across countries. While China and Korea extend explicit tax incentives to foreign investors, other countries focus on stability and transparency of tax laws. Similarly, while all the countries promote investment in manufacturing and services sector, China stands out with its relaxation for agriculture sector as well. It is, however, apparent that though policies across countries vary in specifics, there is a common element of incentivisation of foreign investment (See Table below).

Table : FDI Policy and Institutional Framework in Select Countries

	Year of Libera lisation	**Objective**	**Incentives**	**Priority Sectors**	**Unique features**
China	**1979**	Transformation of traditional agriculture, promotion of industrialization, infrastructure and export promotion.	Foreign joint ventures were provided with preferential tax treatment. Additional tax benefits to export-oriented joint ventures and those employing advanced technology. Privileged access was provided to supplies of water, electricity and transportation (paying the same price as state-owned enterprises) and to interest-free RMB loans.	Agriculture, energy, transportation, telecommunications, basic raw materials, and high-technology industries.	Setting up of Special Economic Zones
Chile	**1974**	Technology transfer, export promotion and greater domestic competition.	Invariability of tax regime intended to provide a stable tax horizon.	All productive activities and sectors of the economy, except for a few restrictions in areas that include coastal trade, air transport and the mass media.	Does not use tax incentives to attract foreign investment.
Korea	**1998**	Promotion of absorptive capacity and indigenisation of foreign technology through reverse engineering at the outset of industrialisation while restricting both FDI and foreign licensing.	Businesses located in Foreign Investment Zone enjoy full exemption of corporate income tax for five years from the year in which the initial profit is made and 50 percent reduction for the subsequent two years. High-tech foreign investments in the Free Economic Zones are eligible for the full exemption three years and 50 percent for the following two years. Cash grants to high-tech green field investment and R&D investment subject to the government approval.	Manufacturing and services	Loan-based borrowing to an FDI-based development strategy till late1990s.
Malaysia	**1980s**	Export promotion	No specific tax incentives.	Manufacturing and services	Malaysian Industrial Development Authority was

					recognised to be one of the effective agencies in the Asian region
Thailand	**1977**	Technology transfer and export promotion	No specific tax incentives. The Thai Board of Investment has carried out activities under the three broad categories to promote FDI. 1. Image building to demonstrate how the host country is an appropriate location for FDI. 2. Investment generation by targeting investors through various activities. 3. Servicing investors	Manufacturing and services	–

CASE STUDY : CROSS-COUNTRY COMPARISON OF FDI POLICIES – WHERE DOES INDIA STAND?

A true comparison of the policies could be attempted if the varied policies across countries could be reduced to a common comparable index or a measure. Therefore, with a view to examine and analyse 'where does India stand' vis-a-vis other countries at the current juncture in terms of FDI policy framework, the present section draws largely from the results of a survey of 87 economies undertaken by the World Bank in 2009 and published in its latest publication titled 'Investing Across Borders'.

The survey has considered four indicators, viz., 'Investing across Borders', 'Starting a Foreign Business', 'Accessing Industrial Land', and 'Arbitrating Commercial Disputes' to provide assessment about FDI climate in a particular country. **Investing across Borders**indicator measures the degree to which domestic laws allow foreign companies to establish or acquire local firms.**Starting foreign business** indicator record the time, procedures, and regulations involved in establishing a local subsidiary of a foreign company. **Accessing industrial land** indicator evaluates legal options for foreign companies seeking to lease or buy land in a host economy, the availability of information about land plots, and the steps involved in leasing land. **Arbitrating commercial disputes** indicator assesses the strength of legal frameworks for alternative dispute resolution, rules for arbitration, and the extent to which the judiciary supports and facilitates arbitration. India's relative position in terms of these four parameters vis-a-vis major 15 emerging economies, which compete with India in attracting foreign investment, is set out in Tables A and B.

Following key observations could be made from this comparison:

- A comparative analysis among the select countries reveals that countries such as Argentina, Brazil, Chile and the Russian Federation have sectoral caps higher than those of India implying that their FDI policy is more liberal.
- The sectoral caps are lower in China than in India in most of the sectors barring agriculture and forestry and insurance. A noteworthy aspect is that China permits 100 per cent FDI in agriculture while completely prohibits FDI in media. In India, on the other hand, foreign ownership is allowed up to 100 per cent in sectors like 'mining, oil and gas', electricity and 'healthcare and waste management'.

Table A : Investing Across Borders – Sector wise Caps – 2009

Country	Mining, oil and gas	Agri-culture and fore-stry	Light manu-facturing	Tele-commu-nications	Electricity	Bank-ing	Insu-rance	Trans-portation	Media	Cons-truction, tourism and retail	Health-care and waste manage-ment
Argentina	100	100	100	100	100	100	100	79.6	30	100	100
Brazil	100	100	100	100	100	100	100	68	30	100	50
Chile	100	100	100	100	100	100	100	100	100	100	100
China	75	100	75	49	85.4	62.5	50	49	0	83.3	85
India	100	50	81.5	74	100	87	26	59.6	63	83.7	100
Indonesia	97.5	72	68.8	57	95	99	80	49	5	85	82.5
Korea,	100	100	100	49	85.4	100	100	79.6	39.5	100	100
Malaysia	70	85	100	39.5	30	49	49	100	65	90	65
Mexico	50	49	100	74.5	0	100	49	54.4	24.5	100	100
Philippines	40	40	75	40	65.7	60	100	40	0	100	100
Russian	100	100	100	100	100	100	49	79.6	75	100	100
South	74	100	100	70	100	100	100	100	60	100	100
Thailand	49	49	87.3	49	49	49	49	49	27.5	66	49

– India positioned well vis-a-vis comparable counterparts in the select countries in terms of the indicator 'starting a foreign business'. In 2009, starting a foreign business took around 46 days with 16 procedures in India as compared with 99 days with 18 procedures in China and 166 days with 17 procedures in Brazil (Table B).

– In terms of another key indicator, viz., 'accessing industrial land' India's position is mixed. While the ranking in terms of indices based on lease rights and ownership rights is quite high, the time to lease private and public land is one of the highest among select countries at 90 days and 295 days, respectively. In China, it takes 59 days to lease private land and 129 days to lease public land. This also has important bearing on the investment decisions by foreign companies.

– In terms of the indicator 'arbitrating commercial disputes' India is on par with Brazil and the Russian Federation. Although, the strength of laws index is fairly good, the extent of judicial assistance index is moderate.

Table B: Investing Across Borders – Key Indicators 2009

Country	Starting a Foreign Business			Accessing Industrial Land						Arbitrating Commercial Disputes		
	Time (days)	Proce-dures (num-ber)	Ease of establi-shment index (0 = min, 100 = max)	Stren-gth of lease rights index (0 = min, 100 = max)	Stren-gthof owne r-ship rights index (0 = min, 100 = max)	Access to land infor-mation index (0 =min, 100 = max)	Avail-ability of land infor-mation index (0 = min, 100 = max)	Time to lease private land (days)	Time to lease public land (days)	Stren-gth of laws index (0 = min, 100 = max)	Ease of process index (0 = min, 100 = max)	Extent o fjudicial assistance index (0 =min, 100 = max)
Argentina	50	18	65	79.3	100	44.4	85	48	112	63.5	72.2	55.1
Brazil	166	17	62.5	85.7	100	33.3	75	66	180	84.9	45.7	57.2

Chile	29	11	63.2	85.7	100	33.3	80	23	93	94.9	62.8	74.8
China	99	18	63.7	96.4	n/a	50	52.5	59	129	94.9	76.1	60.2
India	46	16	76.3	92.9	87.5	15.8	85	90	295	88.5	67.6	53.4
Indonesia	86	12	52.6	78.6	n/a	21.4	85	35	81	95.4	81.8	41.3
Korea,	17	11	71.1	85.7	100	68.4	70	10	53	94.9	81.9	70.2
Malaysia	14	11	60.5	78.5	87.5	23.1	85	96	355	94.9	81.8	66.7
Mexico	31	11	65.8	81.3	100	33.3	90	83	151	79.1	84.7	52.7
Philippines	80	17	57.9	68.8	n/a	23.5	87.5	16	n/a	95.4	87	33.7
Russian	31	10	68.4	85.7	100	44.4	90	62	231	71.6	76.1	76.6
South	65	8	–	84.5	100	47.4	85	42	304	82.4	79	94.5
Thailand	34	9	60.5	80.7	62.5	27.8	70	30	128	84.9	81.8	40.8

Thus, a review of FDI policies in India and across major economics suggests that though India's policy stance in terms of access to different sectors of the economy, repatriation of dividend and norms for owning equity are comparable to that of other economics, policy in terms of qualitative parameters such as 'time to lease private land', 'access to land information' and 'Extent of Judicial assistance' are relatively more conservative. Since time taken to set up a project adds to the cost and affect competitiveness, an otherwise fairly liberal policy regime may turn out to be less competitive or economically unviable owing to procedural delays. Thus, latter may affect the cross border flow of investible funds.

LESSON ROUND UP

- MNC is a corporation that has its facilities and other assets in at least one country other than its home country. Such companies have offices and/or factories in different countries and usually have a centralized head office where they co-ordinate global management.
- The Operations of a Multinational Corporation (MNC) extend beyond the country in which it is incorporated.
- Its headquarters are located in one country (home country) and in addition it carries on business in other countries (host country).
- Foreign Direct Investment means "cross border investment made by a resident in one economy in an enterprise in another economy, with the objective of establishing a lasting interest in the investee economy.
- FDI is also described as "investment into the business of a country by a company in another country".
- FDI is a major source of external finance which means that countries with limited amounts of capital can receive finance beyond national borders from wealthier countries.
- The Department of Industrial Policy & Promotion is the nodal Department for formulation of the policy of the Government on Foreign Direct Investment (FDI).
- Foreign Direct Investment (FDI) in India is undertaken in accordance with the FDI Policy which is formulated and announced by the Government of India.
- Latest Consolidated FDI policy was released with effect from 5th April 2013 with the intent and objective of the Government of India to attract and promote foreign direct investment in order to supplement domestic capital, technology and skills, for accelerated economic growth.

- An Indian company may receive Foreign Direct Investment under the two routes: **Automatic Route and Government Route**
- FDI is prohibited under the Government Route as well as the Automatic Route in the Atomic Energy, Lottery Business, Gambling and Betting, Business of Chit Fund, Nidhi Company, Agricultural, Housing and Real Estate business, Trading in Transferable Development Rights (TDRs)and Manufacture of cigars.

SELF TEST QUESTIONS

1. Explain the meaning and forms of multinational corporations.
2. What are the criticisms of multinational corporations?
3. A multinational corporation has to face various cultural issues – explain.
4. Why is FDI important? Explain the advantages and disadvantages of FDI.
5. Write a short note on recent trends in FDI in India.
6. Explain how FDI policy is formulated in India and its importance.
7. What are the routes under which FDI can enter India?
8. In which sectors of Indian economy FDI is not allowed.
9. What are the key changes in consolidated FDI policy 2013 as compared to earlier FDI policy?
10. Write a short note on:
    - Role of Department of Industrial Policy & Promotion
    - Foreign Investment Implementation Authority (FIIA)

Lesson 4
Foreign Trade Policy and Procedures Part I – Export Promotion

LESSON OUTLINE

- Foreign Trade
- Foreign Trade Policy 2015-2020
- Highlights of the FTP 2015-2020
- Special Economic Zones
- Free Trade and Warehousing Zones
- Institutional Framework for Promotion of Exports
  - Ministry of Commerce
  - Autonomous Bodies
  - Public Sector Undertakings
  - Export Promotion Councils
  - Other Organisation
  - Advisory Bodies
  - Attached & Subordinate Offices
  - Exim Bank of India
- LESSON ROUND UP
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

With increasing integration of the global economy, countries cannot simply rely on domestic market. All the countries in world are engaged in foreign trade to earn foreign exchange. Every country tries to maintain positive balance of trade. For this they try to promote exports from their country. From a longer term perspective, accelerating growth in exports would build up the strength of the economy.

India formulates Foreign Trade Policy every five years to promote exports. Foreign Trade policy provides a framework for increasing exports of goods and services as well as generation of employment and increasing value addition in the country.

In this chapter we will study about the Foreign Trade Policy of India, export promotional measures given in the policy and institutional framework for promotion of export in India.

Export Promotion is a strategy for economic development that stress expanding exports, often through policies that offers encouragement to the exporters with a view to enhance the export of the country.

FOREIGN TRADE

Foreign trade is all about trade among different countries. It is exchange of capital, goods and services across the borders of the countries. Concerning the regulation and promotion of foreign trade, Foreign Trade Policies are announced from time to time in various countries. The countries rich in natural resources export raw materials to other countries whereas some countries that have skilled and qualified manpower export finished materials to other countries. Thus, maintaining a systematic flow of export and import to meet the needs of the developed as well as the underdeveloped nations.

All the countries benefit from the foreign trade as it helps them get their hands on particular materials that are not otherwise available plus put their particular in the global marketplace, consequently resulting in specialization as well as labour division at an international level. Moreover, it brings the nations closer and assists the progress of advanced technology and strengthened economy. Therefore, the policy regarding foreign trade is made with utmost concern.

The international trade policies are aimed at continuity and stability in the market. The policies address upgrades in technology, reduction in transaction costs, market expansion and diversification. Foreign trade helps in stabilizing the prices of goods all the while maintaining the stability of their demand and supply, making the market highly competitive. The FTPs aim to elevate the standard of the goods to be exported so that the exporting countries are acknowledged for the distinctive quality of their products. Employment opportunities are increased because of the mobility of resources and labour required for international trade. There are plentiful jobs in the foreign trade sector including export and import along with other sectors such as banking, insurance, communication and transportation. Thereby, FTPs aim to improve the labour-intensive sectors while coming up with schemes that allow exporters to seek financial support so as to promote their brands, venture out into new markets and hold trade fairs as well as buyer-seller meets.

Regulating the inflow and outflow of good to and from a country, the FTP focuses on earning valuable foreign exchange in the global market. It plays very important role in directing, regulating and promoting the foreign trade.

FOREIGN TRADE POLICY 2015-2020

India's Foreign Trade Policy (FTP) has, conventionally, been formulated for five years at a time and reviewed annually. The focus of the FTP has been to provide a framework of rules and procedures for exports and imports and a set of incentives for promoting exports. The Foreign Trade Policy for 2015-2020 seeks to achieve the following objectives:

- To provide a stable and sustainable policy environment for foreign trade in merchandise and services;
- To link rules, procedures and incentives for exports and imports with other initiatives such as "Make in India , "Digital India and "Skills India to create an "Export Promotion Mission for India;
- To promote the diversification of India's export basket by helping various sectors of the Indian economy to gain global competitiveness with a view to promoting exports;
- To create an architecture for India's global trade engagement with a view to expanding its markets and better integrating with major regions, thereby increasing the demand for India s products and contributing to the government's flagship "Make in India" initiative;
- To provide a mechanism for regular appraisal in order to rationalise imports and reduce the trade imbalance.

There is a clear recognition within Government that exports should not merely be a function of marketable surplus but should reflect a genuine enhancement of economic capacity and development. Through its foreign trade policy, government envisages:

- Employment creation in both manufacturing and services through the generation of foreign trade opportunities
- Zero defect products with a focus on quality and standards;
- A stable agricultural trade policy encouraging the import of raw material where required and export of processed products;
- A focus on higher value addition and technology infusion;
- Investment in agriculture overseas to produce raw material for the Indian industry;
- Lower tariffs on inputs and raw materials; and
- Development of trade infrastructure and provision of production and export incentives.

LEGAL BASIS OF FOREIGN TRADE POLICY (FTP)

The Foreign Trade Policy, 2015-20, is notified by Central Government, in exercise of powers conferred under Section 5 of the Foreign Trade (Development & Regulation) Act, 1992 , as amended. The Foreign Trade Policy, 2015-20 came into force with effect from 01.04.2015

DURATION OF FTP

The Foreign Trade Policy (FTP), 2015-2020, incorporating provisions relating to export and import of goods and services, shall come into force with effect from the date of notification and shall remain in force up to 31st March, 2020, unless otherwise specified. All exports and imports made upto the date of notification shall, accordingly, be governed by the relevant FTP, unless otherwise specified.

AMENDMENT TO FTP

Central Government, in exercise of powers conferred by Section 5 of FT (D&R) Act, 1992, as amended from time to time, reserves the right to make any amendment to the FTP, by means of notification, in public interest.

TRANSITIONAL ARRANGEMENTS

Any License / Authorisation / Certificate / Scrip / any instrument bestowing financial or fiscal benefit issued before commencement of FTP 2015-20 shall continue to be valid for the purpose and duration for which such License/Authorisation/ Certificate / Scrip / any instrument bestowing financial or fiscal benefit Authorisation was issued, unless otherwise stipulated.

In case an export or import that is permitted freely under FTP is subsequently subjected to any restriction or regulation, such export or import will ordinarily be permitted, notwithstanding such restriction or regulation, unless otherwise stipulated. This is subject to the condition that the shipment of export or import is made within the original validity period of an irrevocable commercial letter of credit, established before the date of imposition of such restriction and it shall be restricted to the balance value and quantity available and time period of such irrevocable letter of credit. For operationalising such irrevocable letter of credit, the applicant shall have to register the Letter of Credit with jurisdictional Regional Authority (RA) against computerized receipt, within 15 days of the imposition of any such restriction or regulation.

HIGHLIGHTS OF THE FTP 2015-2020

Export from India Schemes

The objective of the Export from India Schemes is to provide rewards to exporters to offset infrastructural inefficiencies and associated costs involved and to provide exporters a level playing field. There shall be following two schemes for exports of Merchandise and Services respectively:

(i) Merchandise Exports from India Scheme (MEIS).

(ii) Service Exports from India Scheme (SEIS).

Merchandise Exports from India Scheme (MEIS)

Objective of Merchandise Exports from India Scheme (MEIS) is to offset infrastructural inefficiencies and associated costs involved in export of goods/products, which are produced/manufactured in India, especially those having high export intensity, employment potential and thereby enhancing India's export competitiveness.

Rewards for export of notified goods to notified markets under 'Merchandise Exports from India Scheme (MEIS) shall be payable as percentage of realized FOB value (in free foreign exchange). The debits towards basic customs duty in the transferable reward duty credit scrips would also be allowed adjustment as duty drawback. At present, only the additional duty of customs / excise duty / service tax is allowed adjustment as CENVAT credit or drawback, as per Department of Revenue rules

Service Exports from India Scheme (SEIS)

Served From India Scheme (SFIS) has been replaced with Service Exports from India Scheme (SEIS). SEIS shall apply to 'Service Providers located in India' instead of 'Indian Service Providers'. Thus SEIS provides for rewards to all Service providers of notified services, who are providing services from India, regardless of the constitution or profile of the service provider.

The rate of reward under SEIS would be based on net foreign exchange earned. The reward issued as duty credit scrip, would no longer be with actual user condition and will no longer be restricted to usage for specified types of goods but be freely transferable and usable for all types of goods and service tax debits on procurement of services / goods. Debits would be eligible for CENVAT credit or drawback.

Incentives under Export from India Schemes (MEIS & SEIS) also available to units located in Special Economic Zones (SEZs).

Duty credit scrips to be freely transferable and usable for payment of custom duty, excise duty and service tax

- All scrips issued under MEIS and SEIS and the goods imported against these scrips would be fully transferable.
- Scrips issued under Exports from India Schemes can be used for the following:-
  - (i) Payment of customs duty for import of inputs / goods including capital goods
  - (ii) Payment of excise duty on domestic procurement of inputs or goods, including capital goods as per DoR notification.
  - (iii) Payment of service tax on procurement of services as per DoR notification.
- Basic Customs Duty paid in cash or through debit under Duty Credit Scrip can be taken back as Duty Drawback as per DoR Rules, if inputs so imported are used for exports

Status Holders

- Business leaders who have excelled in international trade and have successfully contributed to country's foreign trade are proposed to be recognized as Status Holders and given special treatment and privileges to facilitate their trade transactions, in order to reduce their transaction costs and time.
- The nomenclature of Export House, Star Export House, Trading House, Star Trading House, Premier Trading House certificate has been changed to One, Two, Three, Four, Five Star Export House.

– The criteria for export performance for recognition of status holder have been changed from Rupees to US dollar earnings.

– Manufacturers who are also Status Holders will be enabled to self-certify their manufactured goods as originating from India with a view to qualify for preferential treatment under different Preferential Trading Agreements [PTAs], Free Trade Agreements [FTAs], Comprehensive Economic Cooperation Agreements [CECAs] and Comprehensive Economic Partnerships Agreements [CEPAs] which are in operation. They shall be permitted to self-certify the goods as manufactured as per their Industrial Entrepreneur Memorandum (IEM) / Industrial Licence (IL)/ Letter of Intent (LOI).

Boost to "Make in India"

Reduced Export Obligation (EO) for domestic procurement under Export Promotion Capital Goods Scheme:

Specific Export Obligation under Export Promotion Capital Goods scheme, in case capital goods are procured from indigenous manufacturers, which is currently 90% of the normal export obligation (6 times at the duty saved amount) has been reduced to 75%, in order to promote domestic capital goods manufacturing industry

Higher level of rewards under Merchandise Exports from India Scheme for export items with high domestic content and value addition.

It is proposed to give higher level of rewards to products with high domestic content and value addition, as compared to products with high import content and less value addition.

Online filing of documents/ applications and Paperless trade in 24x7 environment

Director General of Foreign Trade (DGFT) already provides facility of Online filing of various applications under FTP by the exporters/importers. However, certain documents like Certificates issued by Chartered Accountants/ ***Company Secretary*** / Cost Accountant etc. have to be filed in physical forms only.

In order to move further towards paperless processing of reward schemes, it has been decided to develop an online procedure to upload digitally signed documents by Chartered Accountant / ***Company Secretary*** / Cost Accountant. In the new system, it will be possible to upload online documents like annexure attached to ANF 3B, ANF 3C and ANF 3D, which are at present signed by these signatories and submitted physically.

As a measure of ease of doing business, landing documents of export consignment as proofs for notified market can be digitally uploaded in the following manner:-

– Any exporter may upload the scanned copy of Bill of Entry under his digital signature.

– Status holders falling in the category of Three Star, Four Star or Five Star Export House may upload scanned copies of documents.

Simplification of procedures/processes, digitisation and e-governance

– Under Export Promotion Capital Goods (EPCG) scheme, obtaining and submitting a certificate from an independent Chartered Engineer, confirming the use of spares, tools, refractory and catalysts imported for final redemption of EPCG authorizations has been dispensed with.

– At present, the EPCG Authorisation holders are required to maintain records for 3 years after redemption of Authorisations. Now the EPCG Authorization Holders shall be required to maintain records for a period of *two years* only. Government's endeavour is to gradually phase out this requirement as the relevant records such as Shipping Bills, e-BRC are likely to be available in electronic mode which can be archived and retrieved whenever required.

– Exporter Importer Profile: Facility has been created to upload documents in Exporter/Importer Profile. There will be no need to submit copies of permanent records/ documents (e.g. IEC, Manufacturing licence, RCMC, PAN etc.) repeatedly with each application, once uploaded.

– Communication with Exporters/Importers: Certain information, like mobile number, e-mail address etc. has been added as mandatory fields, in IEC data base. This information once provided by exporters, would help in better communication with exporters. SMS/ email would be sent to exporters to inform them about issuance of authorisations or status of their applications.

– Online message exchange with Central Board of Direct Taxes(CBDT) and Ministry of Corporate Affairs(MCA) : It has been decided to have on line message exchange with CBDT for PAN data and with Ministry of Corporate Affairs for CIN and DIN data. This integration would obviate the need for seeking information from IEC holders for subsequent amendments/ updation of data in IEC data base.

– Communication with Committees of DGFT: For faster and paperless communication with various committees of DGFT, dedicated e- mailaddresses have been provided to each Norms Committee, Import Committee and Pre-Shipment Inspection Agency for faster communication.

New initiatives for Export Oriented Undertakings (EOUs), Electronic Hardware Technology Parks (EHTPs) and Software Technology Parks(STPs)

– EOUs, EHTPs, STPs have been allowed to share infrastructural facilities among themselves. This will enable units to utilize their infrastructural facilities in an optimum way and avoid duplication of efforts and cost to create separate infrastructural facilities in different units.

– Inter unit transfer of goods and services have been allowed among EOUs, EHTPs, STPs, and BTPs. This will facilitate group of those units which source inputs centrally in order to obtain bulk discount. This will reduce cost of transportation, other logistic costs and result in maintaining effective supply chain.

– EOUs have been allowed facility to set up Warehouses near the port of export. This will help in reducing lead time for delivery of goods and will also address the issue of un- predictability of supply orders.

– STP units, EHTP units, software EOUs have been allowed the facility to use all duty free equipment/ goods for training purposes. This will help these units in developing skills of their employees.

– 100% EOU units have been allowed facility of supply of spares/ components up to 2% of the value of the manufactured articles to a buyer in domestic market for the purpose of after sale services.

– At present, in a period of 5 years EOU units have to achieve Positive Net Foreign Exchange Earning (NEE) cumulatively. Because of adverse market condition or any ground of genuine hardship, then such period of 5 years for NFE completion can be extended by one year.

– Time period for validity of Letter of Permission (LOP) for EOUs/EHTP/ STPI/BTP Units has been revised for faster implementation and monitoring of projects. Now, LOP will have an initial validity of 2 years to enable the unit to construct the plant and install the machinery. Further extension can be granted by the Development Commissioner up to one year. Extension beyond 3 years of the validity of LOP, can be granted, in case unit has completed 2/3rd of activities, including the construction activities.

– At present, EOUs/EHTP/STPI units are permitted to transfer capital goods to other EOUs, EHTPs, STPs, SEZ units. Now a facility has been provided that if such transferred capital goods are rejected by the recipient, then the same can be returned to the supplying unit, without payment of duty.

– A simplified procedure will be provided to fast track the de-bonding / exit of the STP/ EHTP units. This will save time for these units and help in reduction of transaction cost.

– EOUs having physical export turnover of Rs.10 crore and above, have been allowed the facility of fast track clearances of import and domestic procurement. They will be allowed fast tract clearances of goods, for export production, on the basis of pre- authenticated procurement certificate, issued by customs/central excise authorities.

e-Commerce Exports

– Goods falling in the category of handloom products, books / periodicals, leather footwear, toys and customized fashion garments, having FOB value up to Rs.25000 per consignment (finalized using e-Commerce platform) shall be eligible for benefits under FTP. Such goods can be exported in manual mode through Foreign Post Offices at New Delhi, Mumbai and Chennai.

– Export of such goods under Courier Regulations shall be allowed manually on pilot basis through Airports at Delhi, Mumbai and Chennai as per appropriate amendments in regulations to be made by Department of Revenue. Department of Revenue shall fast track the implementation of EDI mode at courier terminals.

Duty Exemption

Imports against Advance Authorization shall also be eligible for exemption from Transitional Product Specific Safeguard Duty. In order to encourage manufacturing of capital goods in India, import under EPCG Authorisation Scheme shall not be eligible for exemption from payment of anti-dumping duty, safeguard duty and transitional product specific safeguard duty.

Quality Complaints and Trade Disputes

In an endeavour to resolve quality complaints and trade disputes, between exporters and importers, a new chapter, namely, Chapter on Quality Complaints and Trade Disputes has been incorporated in the Foreign Trade Policy. For resolving such disputes at a faster pace, a Committee on Quality Complaints and Trade Disputes (CQCTD) is being constituted in 22 offices and would have members from EPCs/FIEOs/APEDA/EICs.

SPECIAL ECONOMIC ZONE

India was one of the first in Asia to recognize the effectiveness of the Export Processing Zone (EPZ) model in promoting exports, with Asia's first EPZ set up in Kandla in 1965. With a view to overcome the shortcomings experienced on account of the multiplicity of controls and clearances; absence of world-class infrastructure, and an unstable fiscal regime and with a view to attract larger foreign investments in India, the Special Economic Zones (SEZs) Policy was announced in April 2000.

This policy intended to make SEZs an engine for economic growth supported by quality infrastructure complemented by an attractive fiscal package, both at the Centre and the State level, with the minimum possible regulations. SEZs in India functioned from 1.11.2000 to 09.02.2006 under the provisions of the Foreign Trade Policy and fiscal incentives were made effective through the provisions of relevant statutes.

To instil confidence in investors and signal the Government's commitment to a stable SEZ policy regime and with a view to impart stability to the SEZ regime thereby generating greater economic activity and employment through the establishment of SEZs, a comprehensive draft SEZ Bill prepared after extensive discussions with the stakeholders. A number of meetings were held in various parts of the country both by the Minister for Commerce and Industry as well as senior officials for this purpose. The Special Economic Zones Act, 2005, was passed by Parliament in May, 2005 which received Presidential assent on the 23rd of June, 2005. The draft SEZ Rules were widely discussed and put on the website of the Department of Commerce offering suggestions/ comments. Around 800 suggestions were received on the draft rules. After extensive consultations, the SEZ Act, 2005, supported by SEZ Rules, came into effect on 10th February, 2006, providing for drastic simplification of procedures and for single window clearance on matters relating to central as well as state governments.

The main objectives of the SEZ Act are:

(a) generation of additional economic activity

(b) promotion of exports of goods and services;

(c) promotion of investment from domestic and foreign sources;

(d) creation of employment opportunities;

(e) development of infrastructure facilities;

It is expected that this will trigger a large flow of foreign and domestic investment in SEZs, in infrastructure and productive capacity, leading to generation of additional economic activity and creation of employment opportunities.

The SEZ Act 2005 envisages key role for the State Governments in Export Promotion and creation of related infrastructure. A Single Window SEZ approval mechanism has been provided through a 19 member inter-ministerial SEZ Board of Approval (BoA). The applications duly recommended by the respective State Governments/UT Administration are considered by this BoA periodically. All decisions of the Board of approvals are with consensus.

The SEZ Rules provide for different minimum land requirement for different class of SEZs. Every SEZ is divided into a processing area where alone the SEZ units would come up and the non-processing area where the supporting infrastructure is to be created.

The SEZ Rules provide for:

- Simplified procedures for development, operation, and maintenance of the Special Economic Zones and for setting up units and conducting business in SEZs;
- Single window clearance for setting up of an SEZ
- Single window clearance for setting up a unit in a Special Economic Zone;
- Single Window clearance on matters relating to Central as well as State Governments;
- Simplified compliance procedures and documentation with an emphasis on self certification

Approval Mechanism

The developer submits the proposal for establishment of SEZ to the concerned State Government. The State Government has to forward the proposal with its recommendation within 45 days from the date of receipt of such proposal to the Board of Approval. The applicant also has the option to submit the proposal directly to the Board of Approval.

The Board of Approval has been constituted by the Central Government in exercise of the powers conferred under the SEZ Act. All the decisions are taken in the Board of Approval by consensus. The Board of Approval has 19 Members. Its constitution is as follows:

(1) Secretary, Department of Commerce	Chairman
(2) Member, CBEC	Member
(3) Member, IT, CBDT	Member
(4) Joint Secretary (Banking Division), Department of Economic Affairs, Ministry of Finance	
(5) Joint Secretary (SEZ), Department of Commerce	Member
(6) Joint Secretary, DIPP	Member
(7) Joint Secretary, Ministry of Science and Technology	Member
(8) Joint Secretary, Ministry of Small Scale Industries and Agro and Rural Industries	Member
(9) Joint Secretary, Ministry of Home Affairs	Member
(10) Joint Secretary, Ministry of Defence	Member

(11)	Joint Secretary, Ministry of Environment and Forests	Member
(12)	Joint Secretary, Ministry of Law and Justice	Member
(13)	Joint Secretary, Ministry of Overseas Indian Affairs	Member
(14)	Joint Secretary, Ministry of Urban Development	Member
(15)	A nominee of the State Government concerned	Member
(16)	Director General of Foreign Trade or his nominee	Member
(17)	Development Commissioner concerned	Member
(18)	A professor in the Indian Institute of Management or the Indian Institute of Foreign Trade	Member
(19)	Director or Deputy Sectary, Ministry of Commerce and Industry, Department of Commerce	Member Scretary

Administrative set up

The functioning of the SEZs is governed by a three tier administrative set up. The Board of Approval is the apex body and is headed by the Secretary, Department of Commerce. The Approval Committee at the Zone level deals with approval of units in the SEZs and other related issues. Each Zone is headed by a Development Commissioner, who is ex-officio chairperson of the Approval Committee.

Once an SEZ has been approved by the Board of Approval and Central Government has notified the area of the SEZ, units are allowed to be set up in the SEZ. All the proposals for setting up of units in the SEZ are approved at the Zone level by the Approval Committee consisting of Development Commissioner, Customs Authorities and representatives of State Government. All post approval clearances including grant of importer-exporter code number, change in the name of the company or implementing agency, broad banding diversification, etc. are given at the Zone level by the Development Commissioner. The performance of the SEZ units are periodically monitored by the Approval Committee and units are liable for penal action under the provision of Foreign Trade (Development and Regulation) Act, in case of violation of the conditions of the approval.

Facilities and Incentives

The incentives and facilities offered to the units in SEZs for attracting investments into the SEZs, including foreign investment include:-

- Duty free import/domestic procurement of goods for development, operation and maintenance of SEZ units
- 100% Income Tax exemption on export income for SEZ units under Section 10AA of the Income Tax Act for first 5 years, 50% for next 5 years thereafter and 50% of the ploughed back export profit for next 5 years.
- Exemption from minimum alternate tax under section 115JB of the Income Tax Act.
- External commercial borrowing by SEZ units upto US $ 500 million in a year without any maturity restriction through recognized banking channels.
- Exemption from Central Sales Tax.
- Exemption from Service Tax.
- Single window clearance for Central and State level approvals.
- Exemption from State sales tax and other levies as extended by the respective State Governments.

The major incentives and facilities available to SEZ developers include:-

- Exemption from customs/excise duties for development of SEZs for authorized operations approved by the BOA.
- Income Tax exemption on income derived from the business of development of the SEZ in a block of 10 years in 15 years under Section 80-IAB of the Income Tax Act.
- Exemption from minimum alternate tax under Section 115 JB of the Income Tax Act.
- Exemption from dividend distribution tax under Section 115O of the Income Tax Act.
- Exemption from Central Sales Tax (CST).
- Exemption from Service Tax (Section 7, 26 and Second Schedule of the SEZ Act).

Setting Up of SEZ

Any individual, co-operative society, company or partnership firm can file an application for setting up of Special Economic Zone. The application is to be made in Form-A (attached below) to the concerned State Government and the Board of Approval (BOA) in the Department of Commerce, Government of India. However the application would be considered by the BOA only when the State Government recommendation is received.

Minimum area requirements for setting up a SEZ are as follows:

Multi Sector SEZ	1000 hectares
Sector Specific SEZ	100 hectares
FTWZ	40 hectares
IT/ITES/handicrafts SEZ Bio-technology/ non-conventional energy/gems and jewellery Sector	10 hectares

Once the BOA gives formal approval and the concerned Development Commissioner gives an inspection report certifying the contiguity and vacancy of the area, the area is notified as SEZ.

FREE TRADE AND WAREHOUSING ZONES

The Government of India (GoI) had announced in the Foreign Trade Policy 2004-09 to set up Free Trade and Warehousing Zones (FTWZ) to create trade related infrastructure to facilitate the import and export of goods and services with freedom to carry out trade transactions in free currency. The Free Trade and Warehousing Zones (FTWZ) is a special category of Special Economic Zone and is governed by the provisions of the SEZ Act and the Rules.

- FTWZ is a 'Sanitized Zone' designated as Foreign Territory for carrying on business.
- FTWZ's are envisaged to be Integrated Zones & to be used as'International Trading Hubs'.
- Each Zone would provide 'World Class' Infrastructure for :
  - Warehousing for various kinds of products
  - Handling and Transportation Equipment
  - Commercial office space
  - All related utilities - telecom, power, water, etc
  - One stop clearance of Import and Export of goods
- FTWZ would be a key Link in Logistic and Global Supply chains - servicing both India and the Globe.

Features

- Logistics and Distribution Centre
- Provides "Free Zone" environment
- Enables efficient operational environment for trade facilitation
- Integrates various aspects of logistics operations
- Provision of high quality infrastructure
- 100% Foreign Direct Investment is permitted in development and establishment of FTWZ
- FTWZ is a deemed foreign territory and all equipments and materials sourced from the Domestic Tariff Area will be considered as Imports by the FTWZ and vice versa
- Minimum size of the warehousing stipulated at 1 lakh sq mtrs
- All benefits available to the SEZs shall be applicable to the FTWZs
- The FTWZ shall be under the administrative control of the Development Commissioner (DC)

Benefits

1. Fiscal and Regulatory Benefits

- Tax Benefits :Income tax (section 80IA) and Service Tax exemptions for developers and users of the zone ~ reduces logistics costs for users of the zone.
- Duty Deferment Benefits :Custom Duty deferment benefits for products requiring longer storage time.
- Excise Duty Exemptions : Excise duty exemption for products sourced from the domestic markets, including goods, spares, DG sets, packing materials, etc.

2. Infrastructure Benefits

- Single Product Storage Facilities : Assist in meeting specific warehousing requirement for each product category e.g. different sections for storage of tea and coffee, etc.
- Shared warehousing : Availability of temporary storage facilities to enable users to meet short term demand without incurring significant costs (e.g. leasing space for a year to meet 2/3 months demand)
- Shared Equipments : Ability of users to save on capital investments by leasing equipments provided by the zone.

3. Administration Benefits

- Delivery Time : Reduction in custom clearance time and better logistics connectivity leading to improved delivery time.
- Support Facilities and Effective Management : Provision of efficient management services and international expertise along with support facilities such as banking, insurance etc.

4. Other Benefits

- Export oriented
- FDI inflow
- Employment potential.
- Competitiveness of industries

- Attractiveness of support/ancillary industries
- Boost to all-round economic activity

Facilities available in a FTWZ

- Customised categorised warehouses ~ chemicals, food, electronics, oil, etc.
- Sophisticated freezer / cooler facilities
- Break bulk, containerised, and dry cargo storage facilities
- Controlled humidity warehouses
- Enhanced transportation facilities
- World-class information system for cargo tracking etc.
- Office space
- Support facilities and amenities like medical facility, canteen services, business centres

Some FTWZ in India

- Free Trade Warehousing Private Limited (FTWPL)
- Arshiya International Limited (AIL)
- Balaji Infra Projects Limited (BIPL)
- FAB City SPV (India)
- LMJ Warehousing [Gujarat]
- Jafza Chennai Business parks [Gujarat]
- Shipco Infrastructure [Karnataka]
- Chiplun Infrastructure Private Limited
- DLF Unviersal
- J.Matadee Eco Parks Private Limited
- Jhunjhunwala Vanaspati

INSTITUTIONAL FRAMEWORK FOR PROMOTION OF EXPORTS

The organisational structure for promotion of exports includes a number of councils and organisations set up during the post- independence period. These include the Export promotion councils, Commodity Boards, Agriculture and Processed Food Products Export Development Authority, Export Houses, The central advisory council on trade, The Trade Development Authority, The Indian Institute of Packaging, Trade fair Authority of India, The Federation of Indian Export Organisation, The Export Inspection Council. Several export-promoting organizations are established to promote exports. A brief description of all such organisations which promote exports in India is given below:

(1) Ministry of Commerce

(2) Autonomous Bodies under Ministry of Commerce
   - Commodity Boards
   - Marine Products Export Development Authority

- Agricultural and Processed Food Products Export Development Authority
- Export Inspection Council
- Indian Institute of Foreign Trade
- Indian Institute of Packaging

(3) Public Sector Undertakings under Ministry of Commerce

- State Trading Corporation (STC)
- MMTC Limited
- PEC Limited
- Export Credit Guarantee Corporation of India Limited
- India Trade Promotion Organisation

(4) Export Promotion Councils

(5) Other Organisations under Ministry of Commerce

- Federation of Indian Export Organisations
- Indian Council of Arbitration
- Indian Diamond Institute
- Footwear Design & Development Institute (FDDI)
- National Centre for Trade Information
- Price Stabilization Fund Trust
- GS1-India

(6) Advisory Bodies

- Board of Trade
- Inter State trade Council

(7) Attached and Subordinate Offices

- Directorate General of Foreign Trade
- Directorate General of Supplies and Disposals (DGS & D)
- Directorate General of Anti-Dumping & Allied Duties (DGAD)
- Directorate General of Commercial Intelligence and Statistics, Kolkata
- Special Economic Zones
- Pay & Account Office (Supply, Commerce & Textiles)

(8) Exim Bank of India

MINISTRY OF COMMERCE

The Department of Commerce, Government of India is the most important organ concerned with the regulation, development and promotion of India's international trade and commerce through formulation of appropriate

international trade & commercial policy and implementation of the various provisions thereof. The basic role of the Department is to facilitate the creation of an enabling environment and infrastructure for accelerated growth of international trade. The Department formulates, implements and monitors the Foreign Trade Policy (FTP) which provides the basic framework of policy and strategy to be followed for promoting exports and trade. The Trade Policy is periodically reviewed to incorporate changes necessary to take care of emerging economic scenarios both in the domestic and international economy. Besides, the Department is also entrusted with responsibilities relating to multilateral and bilateral commercial relations, Special Economic Zones, state trading, export promotion and trade facilitation, and development and regulation of certain export oriented industries and commodities.

The Department is headed by a Secretary who is assisted by an Additional Secretary & Financial Adviser, three Additional Secretaries, thirteen Joint Secretaries and Joint Secretary level officers and a number of other senior officers. Keeping in view the large increase in workload in matters related to the World Trade Organization (WTO), Regional Trade Agreements (RTAs), Free Trade Agreements (FTAs), Special Economic Zones (SEZs), Joint Study Groups (JSGs) etc, two posts each of Joint Secretaries and Directors were created in the Department during 2008-09.

The Department is functionally organized into the following eight Divisions:

1. Administration and General Division
2. Finance Division
3. Economic Division
4. Trade Policy Division
5. Foreign Trade Territorial Divisions
6. State Trading & Infrastructure Division
7. Supply Division
8. Plantation Division.

The various offices/ organizations under the administrative control of the Department are: (A) three Attached Offices, (B) eleven Subordinate Offices, (C) ten Autonomous Bodies, (D) five Public Sector Undertakings, (E) Advisory Bodies, (F) fourteen Export Promotion Councils and (G) other Organizations.

Subject matter of Ministry includes:

I. International Trade
   - International Trade and Commercial Policy including tariff and non-tariff barriers.
   - International Agencies connected with Trade Policy (eg. UNCTAD, ESCAP, ECA, ECLA, EEC, EFTA, GATT/WTO, ITC and CFC).
   - International Commodity Agreements other than agreements relating to wheat, sugar, jute and cotton.
   - International Customs Tariff Bureau including residuary work relating to the Tariff Commission.

II. Foreign Trade (Goods & Services)
   - All matters relating to foreign trade.
   - Import and Export Trade Policy and Control excluding matters relating to Import of feature films; Export of Indian films- both feature length and shorts; and Import and distribution of cine-film (unexposed) and other goods required by the film industry.

III. State Trading

Policies of state trading and performance of organizations established for the purpose and including –

– The State Trading Corporation of India Limited and its subsidiary, STCL Ltd.

– Projects & Equipment Corporation of India Limited (PEC);

– India Trade Promotion Organization and its subsidiaries; and

– Minerals and Metals Trading Corporation and its subsidiaries.

– Production, distribution (for domestic consumption and exports) and development of plantation crops, tea, coffee, rubber, spices, tobacco and cashew.

– Processing and distribution for domestic consumption and exports of instant tea and instant coffee

– Commodity baords

(a) Tea Board.

(b) Coffee Board.

(c) Rubber Board.

(d) Spices Board.

(e) Tobacco Board.

IV. Management of Certain Services

– Cadre Management of Indian Trade Service and all matters pertaining to training, career planning and manpower planning for the service.

– Cadre Management of Indian Supply Service and all matters pertaining to training, career planning and manpower planning for the service.

– Cadre Management of Indian Inspection Service and all matters pertaining to training, career planning and manpower planning for the service.

V. Special Economic Zones

All matters relating to development, operation and maintenance of special economic zones and units in special economic zones, including export and import policy, fiscal regime, investment policy, other economic policy and regulatory framework.

Note: All fiscal concessions and policy issues having financial implications are decided with the concurrence of the Ministry of Finance or failing such concurrence with the approval of the Cabinet

VI. Export Products and Industries and Trade Facilitation

– Gems and Jewellery.

– Matters relating to Export Promotion Board, Board of Trade and International Trade Advisory Committee.

– Matters relating to concerned Export Promotion Councils/Export Promotion Organizations.

– Indian Institute of Foreign Trade and Indian Institute of Packaging.

– Indian Diamond Institute and Footwear Design and Development Institute.

– Coordination for export infrastructure.

– Development and expansion of export production in relation to all commodities, products, manufacturers and semi-manufacturers including -

- agricultural produce within the meaning of the Agricultural Produce (Grading and Marking) Act, 1937 (1 of 1937);
- marine products;
- industrial products (engineering goods, chemicals, plastics, leather products, etc.);
- fuels, minerals & mineral products; and specific export oriented products including plantation crops, etc. but excluding jute products and handicrafts.

– All organizations and institutions connected with the provision of services relating to the export effort including -

- Export Credit and Export Insurance including Export Credit Guarantee Corporation Limited;
- Export Inspection Council Standards including Quality Control;
- Directorate General of Commercial Intelligence and Statistics; and
- Free Trade-Zones.
- Projects and programmes for stimulating and assisting the export efforts.

VII. Attached and Subordinate Offices

- Directorate General of Foreign Trade.
- Directorate General of Supplies and Disposals.
- Directorate General of Anti-Dumping and Allied Duties and related matters.
- Directorate General of Commercial Intelligence and Statistics.

VIII. Statutory Bodies

- Marine Products Export Development Authority.
- Agricultural and Processed Food Products Export Development Authority.

IX. Miscellaneous

Purchase and inspection of stores for Central Government Ministries/ Departments including their attached and subordinate offices and Union Territories, other than the items of purchase and inspection of stores which are delegated to other authorities by general or special order.

AUTONOMOUS BODIES/ PUBLIC SECTOR UNDERTAKINGS/ EXPORT PROMOTION COUNCILS/ OTHER ORGANIZATIONS UNDER MINISTRY OF COMMERCE

Commodity Boards

1. Tea Board : The Tea Board was constituted as a statutory body on 1st April, 1954 under Section (4) of Tea Act 1953. The Board, with its Head Office at Kolkata, is headed by a Chairman. It has 30 Members drawn from different stake holders of the tea Industry and fifteen regional/sub-regional offices. The Board functions as an apex body for the all round development of the tea Industry. With a view to promote the export of Tea, the Board established three offices abroad viz. London, Moscow and Dubai. The primary functions of the Tea Board include rendering financial and technical assistance to tea producers, manufacturers, growers and also help marketing of tea within the country and abroad. Research activities at different Research Institutes viz. Tea Research Association (TRA), United Planters' Association of Southern India-Tea Research Foundation (UPASI-TRF), are funded for augmentation of Tea Production and Quality improvement. It also regulates and controls different marketing activities including that of Tea Auctions and maintains statistical data on production, consumption and export.

2. Coffee Board : The Coffee Board is a statutory organization constituted under the Coffee Act, 1942. The Board, with its Head Office at Bangalore, is headed by a Chairman. It has 33 members, with offices located at Coffee growing areas viz Karnataka, Kerala, Tamil Nadu, Andhra Pradesh, Orissa and North Eastern Region besides Delhi, Guwahati, Mysore, and Chennai. The Board also has a Central Coffee Research Institute at Chikmagalur and Sub/Regional Research Stations at Chettalli, Chundale, Thandigudi, R. V. Nagar, Diphu and Division of Tissue Culture at Mysore. The functions of the Board are primarily directed towards research, extension and development of coffee, domestic and external promotion of coffee, gathering of market intelligence and human resources development.

3. Rubber Board : The Rubber Board is a statutory body constituted under the Rubber Act, 1947 with a view to promote the rubber industry in the country. The Board, with its Head Office is located at Kottayam, comprises of 26 members including the Chairman, who is the Chief Executive. The functions of the Board broadly are undertaking, assisting or encouraging scientific technological and economic research, imparting training to students/growers on improved methods of cultivation, manuring and spraying, rendering technical advice to the rubber growers, improving marketing, collecting statistics from owners of estates, dealers and manufacturers, securing better working conditions, providing/improving amenities and incentives for workers.

4. Spices Board: The Spices Board Act, 1986 assigns to the Spices Board the responsibility of export development of 52 Spices. Some of the major spices among them are Pepper, Chilli, Ginger, Turmeric, Cardamom, Coriander, Cumin, Fennel, Fenugreek, Celery, Vanilla and Saffron. The Board is implementing a number of schemes aimed at export development of Spices with a view to meet international standards and promotion of export of value added Spices. The Board has well-established quality evaluation and upgradation laboratory at Kochi that is engaged in surveying the quality of spices procured form different producing and marketing centres. It offers training for quality upgradation to growers and exporters and undertakes physical, chemical and biological analysis of the samples brought by the exporters.

5. Coconut Development Board : Coconut Development Board (CDB) is a statutory body established under the Ministry of Agriculture, Government of India for the integrated development of coconut cultivation and industry in the country with focus on productivity increase and product diversification.

6. Tobacco Board : The Tobacco Board was constituted in 1976 with the objective of promoting the planned development of the tobacco industry. The Board regulates the production, curing and marketing of FCV tobacco. It also monitors fluctuations in market demand, both domestic and international for FCV tobacco in order to help in devising an appropriate market strategy. In addition, it conducts extension and developmental programmes for the benefit of the growers. In essence, its function is to further the interests of the growers, manufacturers and exporters of FCV tobacco. The 26-Member Board is headquartered in Guntur (Andhra Pradesh) with subordinate offices at Bangalore, 4 Regional Offices and 29 auction platforms.

7. Central Silk Board : Central Silk Board established in 1949 as a statutory body under Govt. of India, is a national organization for overall development of sericulture and silk industry. Its headquarters is located in Bangalore.Disseminate information on exports of Natural Silk Goods and Import of Raw Silk. Guidance to New Entrepreneur Exporters on procedures and formalities. Export and Import Policy relating to silk. Incentives offered by the Govt. of India against exports of silk goods. Imparting technical knowledge on silk manufacturing.

Marine Products Export Development Authority, Cochin

The Marine Products Export Development Authority was set up as a Statutory Body in 1972 under an Act of Parliament (No.13 of 1972). The Authority, with its headquarters at Kochi and field offices in all the Maritime States of India, is headed by a Chairman/Chairperson. The Authority is responsible for development of the marine industry with special focus on marine exports. Besides, it has Trade Promotion Offices at Tokyo (Japan) and New York (USA)

Agricultural and processed Food Products Export Development Authority, New Delhi

The Agricultural and Processed Food Products Export Development Authority (APEDA) was established in 1986 as a Statutory Body under an Act of Parliament. The Authority, with its headquarters at New Delhi, is headed by a Chairman. The Authority has five Regional Offices at Guwahati, Hyderabad, Kolkata, Bangalore & Mumbai and is entrusted with the task of promoting agricultural exports, including the export of processed foods in value added form. APEDA has also been entrusted with monitoring of export of 14 agricultural and processed food product groups listed in the Schedule to the APEDA Act. APEDA has been actively engaged in the development of markets besides upgradation of infrastructure and quality to promote the export of agro products. In its endeavour to promote agro products, APEDA provides financial assistance to the registered exporters under its Schemes for Market Development, Infrastructure Development, Quality Development, Research and Development and Transport Assistance. During the year 2009-10, APEDA has been empowered by an Act of Parliament to enforce the Intellectual Property Right (IPR) of Geographical Indications (GI) for Basmati Rice.

Export Inspection Council

The Export Inspection Council was set up as a Statutory Body on 1st January, 1964 under Section 3 of the Export (Quality Control and Inspection) Act, 1963 to ensure sound development of export trade of India through quality control and inspection and for matters connected therewith. The Council is an advisory body to the Central Government, with its office located at New Delhi and is headed by a Chairman. The Executive Head of the EIC is the Director of Inspection & Quality Control who is responsible for the enforcement of quality control and compulsory pre-shipment inspection of various commodities meant for export and notified by the Government under the Export (Quality Control and Inspection) Act, 1963. The Council is assisted in its functions by the Export Inspection Agencies (EIAs), which are field organizations located at Chennai, Delhi, Kochi, Kolkata and Mumbai and have state-of-art and accredited laboratories with the required logistic support for quality certification activities. These Agencies have a network of thirty six sub-offices and laboratories located at different ports or major industrial centres to back up the pre-shipment inspection and certification activities.

Indian Institute of Foreign Trade, New Delhi

The Indian Institute of Foreign Trade was registered in May, 1963 under the Societies Registration Act, 1860. The Institute, with its head office at New Delhi and one regional branch at Kolkata, is headed by a Director. The Institute has been conferred “Deemed University” status and is engaged in the following activities:-

- Conducting academic courses leading to issue of degrees in International Business & Export Management;
- Training of personnel in international trade;
- Organizing research on issues in foreign trade, marketing research, area surveys, commodity surveys, market surveys; and
- Dissemination of information arising from its activities relating to research and market studies.

Indian Institute of Packaging, Mumbai

The Indian Institute of Packaging was registered in May, 1966 under the Societies Registration Act, 1860. The Institute, with its office located at Mumbai and branch offices at Delhi, Chennai, Kolkata and Hyderabad, is headed by a Director. The main function of the Institute is to undertake research on raw materials for the packaging industry, organize training programmes on packaging technology, consultancy services on packaging problems and stimulate consciousness of the need for good packaging.

PUBLIC SECTOR UNDERTAKINGS UNDER MINISTRY OF COMMERCE

State Trading Corporation of India Limited (STC)

STC was set up on 18th May, 1956, primarily with a view to undertake trade with East European Countries and to supplement the efforts of private trade and industry in developing exports from the country. STC has played an important role in country's economy by arranging imports of essential items of mass consumption (such as wheat, pulses, sugar, etc.) into India and developing exports of a large number of items from India. The core strength of STC lies in handling exports/ imports of bulk agro commodities. During past 4-5 years, STC has diversified into exports of steel raw materials, gold jewellery and imports of bullion, hydrocarbons, minerals, metals, fertilizers, petro-chemicals, etc. Achieving record breaking performances year-after-year, STC is today able to structure and execute trade deals of any magnitude, as per the specific requirement of its customers. STCL Ltd. is a subsidiary of STC. It was initially established in 1982 as Cardamom Trading Corporation Ltd., a Government of India undertaking under the Ministry of Commerce & Industry. The company developed from a solely cardamom trading corporation to become Spices Trading Corporation Ltd., in 1987. With globalization and opening of trade world over, Spices Trading Corporation Ltd. was renamed as STCL Ltd. STCL became a wholly owned subsidiary of the State Trading Corporation of India Ltd. in 1999. STCL is involved in import, export and domestic trading of a varied range of products, both agricultural as well as non-agricultural. STCL, headed by a Chairman, is headquartered in Bangalore.

MMTC Limited

The MMTC Limited (Minerals and Metals Trading Corporation) was created in 1963 as an individual entity on separation from State Trading Corporation of India Ltd. primarily to deal in exports of minerals and ores and imports of non-ferrous metals. In 1970, MMTC took over imports of fertilizer raw materials and finished fertilizers. Over the years import and exports of various other items like steel, diamonds, bullion, etc. were progressively added to the portfolio of the company. Keeping pace with the national economic development, MMTC over the years has grown to become the largest trading organization in India.

PEC Limited

The PEC Ltd (Project and Equipment Corporation of India) was carved out of the STC in 1971-72 to take over the canalized business of STC's railway equipment division, to diversify into turn-key projects especially outside India and to aid & assist in promotion of exports of Indian engineering equipment. With effect from 23rd May, 1990, PEC became a subsidiary of the then newly formed Holding Company, Bharat Business International Ltd. Thereafter, from 27th March, 1991, PEC became an independent company directly owned by Government of India. The main functions of PEC Ltd. includes export of projects, engineering equipment and manufactured goods, defence equipment & stores; import of industrial raw materials, bullion and agro commodities; consolidation of existing lines of business and simultaneously developing new products and new markets; diversification in export of non-engineering items eg. Coal & coke, iron ore, edible oils, steel scraps, etc.; and structuring counter trade/ special trading arrangements for further exports.

Export Credit Guarantee Corporation of India Limited (ECGC)

The Corporation was established in 1957 as the Export Risk Insurance Corporation of India Ltd. Keeping in view the wider role played by the Corporation, the name was changed to Export Credit Guarantee Corporation of India Ltd. (ECGC). The ECGC is the premier organization in the country, which offers credit risk insurance cover to exporters, banks, etc. The primary objective of the Corporation is to promote the country's exports by covering the risk of export on credit. It provides (a) a range of insurance covers to Indian exporters against the risk of non-realization of export proceeds due to commercial or political causes and (b) different types of guarantees to banks and other financial institutions to enable them to extend credit facilities to exporters on liberal basis.

Export Credit Guarantee Corporation of India Limited, was established to strengthen the export promotion drive by covering the risk of exporting on credit. Being essentially an export promotion organization, it functions under the administrative control of the Ministry of Commerce & Industry, Department of Commerce, and Government of India. It is managed by a Board of Directors comprising representatives of the Government, Reserve Bank of India, banking, insurance and exporting community. ECGC is the fifth largest credit insurer of the world in terms of coverage of national exports. The present paid-up capital of the company is Rs.800 crores and authorized capital Rs.1000 crores.

Functions of Export Credit Guarantee Corporation of India Limited:

- Provides a range of credit risk insurance covers to exporters against loss in export of goods and services
- Offers guarantees to banks and financial institutions to enable exporters to obtain better facilities from them
- Provides Overseas Investment Insurance to Indian companies investing in joint ventures abroad in the form of equity or loan

It provides support to exporters in following ways:

- Offers insurance protection to exporters against payment risks
- Provides guidance in export-related activities
- Makes available information on different countries with its own credit ratings
- Makes it easy to obtain export finance from banks/financial institutions
- Assists exporters in recovering bad debts
- Provides information on credit-worthiness of overseas buyers

India Trade Promotion Organization (ITPO)

India Trade Promotion Organization has been formed by merging erstwhile Trade Development Authority (TDA) with Trade Fair Authority of India (TFAI) with effect from 1st January, 1992. India Trade Promotion Organization is the premier trade promotion agency of India and provides a broad spectrum of services to trade and industry so as to promote India's exports. These services include organization of trade fairs and exhibitions in India and abroad, Buyer-Seller Meets, Contact Promotion Programmes apart from information dissemination on products and markets.

EXPORT PROMOTION COUNCIL

The Export Promotion Councils are Non-profit, Autonomous and Professional Bodies registered under the Indian Companies Act or the Societies Registration Act, as the case may be.

Features

- The EPCs are autonomous and regulate their own affairs. However, if the Central Government frames uniform bylaws for the constitution and/or for the transaction of business for EPCs, they shall adopt the same.
- The EPCs shall be required to obtain the approval of the Central Government for participation in trade fairs, exhibitions etc and for sending sales teams/ delegations abroad.
- The Department of Commerce/ Ministry of Textiles of the Government of India, as the case may be, would interact with the Managing Committee of the Council concerned, twice a year, once for approving their annual plans and budget and again for a mid-year appraisal and review of their performance.

- The EPCs should function as professional bodies. For this purpose, executives with a professional background in commerce, management and international marketing and having experience in government and industry should be brought into the EPCs.
- The EPCs may be provided financial assistance by the Central Government.
- The Export Promotion Councils are also the registering authorities under the Export Import Policy, 1997-2002. An exporter may, on application, register and become a member of Export Promotion Council. On being admitted to membership, the applicant shall be granted forthwith Registration-cum- Membership Certificate (RCMC) of the EPC concerned.

Basic Objective

The basic objective of Export Promotion Councils is to promote and develop the exports of the country. Each Council is responsible for the promotion of a particular group of products, projects and services.

Role

- The main role of the EPCs is to project India's image abroad as a reliable supplier of high quality goods and services.
- The EPCs shall encourage and monitor the observance of international standards and specifications by exporters.
- The EPCs shall keep abreast of the trends and opportunities in international markets for goods and services and assist their members in taking advantage of such opportunities in order to expand and diversify exports.

Functions

The Export Promotion Councils perform both advisory and executive functions. The major functions of the EPCs are:

- To provide commercially useful information and assistance to their members in developing and increasing their exports.
- To offer professional advice to their members in areas such as technology up gradation, quality and design improvement, standards and specifications, product development, innovation, etc.
- To organize visits of delegations of its members abroad to explore overseas market opportunities.
- To organize participation in trade fairs, exhibitions and buyer-seller meets in India and abroad.
- To promote interaction between the exporting community and the Government both at the Central and State levels.
- To build a statistical base and provide data on the exports and imports of the country, exports and imports of their members, as well as other relevant international trade data.

Registered Export Promotion Councils

There are at present twelve Export Promotion Councils under the administrative control of the Department of Commerce and nine export promotion councils related to textile sector under the administrative control of Ministry of Textiles. These Councils are registered as non -profit organizations under the Companies Act/Societies Registration Act.

EPCS under the Administrative Control of the Department of Commerce

(1) Engineering Export Promotion Council : The Engineering Export Promotion Council (EEPC) was set up in

1955 under the sponsorship of Ministry of Commerce, Govt. of India, for export promotion of engineering goods, projects and services from India. Initially, it started with a few hundreds of engineering units as a small outfit, with a passage of time it has grown to be the largest Export Promotion Council having membership of nearly 12,000 from amongst large Corporate Houses, Star Trading Houses, Small & Medium Scale Units (SME), Trading Houses, etc.

(2) Project Exports Promotion Council of India : The Ministry of Commerce & Industry, Government of India established project Exports Promotion Council (PEPC) in 1984 (as Overseas Construction Council of India). PEPC in line with the Foreign Trade Policy of the Government of India not only undertakes the necessary export promotion initiatives but also provides necessary technical information, guidance and support to Indian construction and process engineering contractors and consultants – in public or private sector – to set up overseas projects. Besides, PEPC also provides the necessary technical and market information, guidance and export promotion facilitation to the traders/manufacturers of various Project Construction items (excluding steel and cement).

(3) Basic Chemicals, Pharmaceuticals and Cosmetics Export Promotion Council : Basic Chemicals, Pharmaceuticals & Cosmetics Export Promotion Council (CHEMEXCIL), was established in the year 1963 with the objective of making concerted efforts to promote exports of Basic Organic and Inorganic Chemicals, Dyes, Pesticides, Soaps, Detergents, Cosmetics, Toiletries and other products like Agarbattis, Essential, Castor Oil, etc. The Council also has some functional committees which attend to some specialised aspects of Council's work like Projects, Publicity and Exhibitions, Registration and Export Assistance, Budget, etc.

(4) Chemicals and Allied Products Export Promotion Council : CAPEXIL, a non-profit making organization, was setup in March 1958 by the Ministry of Commerce, Government of India to promote export of Chemical and Allied Products from India. And since then has been the voice of Indian business community. CAPEXIL has more than 3500 members across the country. One of the fascinating aspects of CAPEXIL is the overwhelming variety of products it deals with. CAPEXIL sends trade delegation to all major and developing markets around the world, showcases Indian exports all over the world through exhibitions, fairs. CAPEXIL is an ISO 9001: 2000 certified organization.

(5) Council for Leather Exports : The Council for Leather Exports was set up Ministry of Commerce, Government of India, in July 1984 under the Indian Companies Act 1956. The Council is entrusted with export promotion activities and overall development of the Indian leather industry. The Council's activities also include promoting Foreign Direct Investments and Joint Ventures in the Indian leather industry. The CLE creates a bridge between Indian leather exporters and buyers all over the world.

(6) Sports Goods Export Promotion Council : The Government of India established the Sports Goods Export Promotion Council (SGEPC) in 1958 to promote exports of sports goods and toys from India. SGEPC organizes trade promotion activities like Indian participation in International Trade fairs, Visits of Business Delegations, Promotional campaigns in international markets, etc. The council also provides important information to the members on market intelligence, standards & specifications, quality & design, and on any other issue which may directly or indirectly affect the industry.

(7) Gem and Jewellery Export Promotion Council : The Gem & Jewellery Export Promotion Council (GJEPC) has over the years effectively moulded the scattered efforts of individual exporters to make the gem and jewellery sector a powerful engine driving India's export-led growth. This apex body has played a significant role in the evolution of the Indian gem and jewellery industry to its present stature. GJEPC is continuously working towards creating a pool of artisans and designers trained to international standards so as to consolidate the Indian jewellery industry and establish it as a prominent global player in the jewellery segment.

(8) Shellac Export Promotion Council : Shellac Export Promotion Council sponsored by the Ministry of Commerce, Govt. of India, to promote export of Shellac and Lac based products like Shellac, both Hand Made and Machine Made, Dewaxed Shellac, Seedlac, Aleuritic Acid, Bleached Lac and Shellac Wax. Shellac EPC builds a bridge between the Trade and the Government. International developments and Govt. Policies often

dictate the course of exports, Shellac EPC activates its umbrella network to monitor and analyse these trends and accordingly Policy anomalies are either modified or changed in the interests of exports

(9) Cashew Export Promotion Council : The Government of India established the Cashew Export Promotion Council of India (CEPC) in the year 1955. The aim of CEPC is promoting exports of cashew kernels and cashew nut shell liquid from India. The Council provides the necessary institutional framework for performing the different functions that serve to intensify and promote exports of cashew kernels and cashew nut shell liquid.

(10) Plastics Export Promotion Council : The Plastics Export Promotion Council (PLEXCONCIL) sponsored by the Ministry of Commerce & Industry, Department of Commerce, Government of India, represents the exporting community of the Indian Plastics industry. The council represent exporters from the Indian Plastic Industry and our membership comprises over 2000 manufacturers/ exporters exporting a wide range of plastic items ranging from plastic raw materials to finished goods. PLEXCONCIL is involved in export promotional activities like participation in international trade fairs; sponsoring delegations to target markets; inviting business delegations from the overseas to India; organising buyer-seller meets both in India and the overseas and servicing the needs of its members.

(11) Export Promotion Council for EOUs & SEZ Units : The Export Promotion Council for EOUs and SEZ Units (EPCES) has been set- up to service the export promotional needs of 100% Export Oriented Units (EOUs), Special Economic Zone (SEZ) Units and Agri Economic Zones in the country. EPCES represents EOU/SEZ Sector, which has over 2900 EOUs/SEZ Units, spread all over the country. This Council is a multi-product and scheme specific Export Promotion Council. The EOUs/SEZ Units cover major industrial sectors like Textiles, Garments & Yarn, Food & Agro Products, Electronics & Software, Chemical, Engineering, Minerals, Granite, etc.

(12) Pharmaceutical Export Promotion Council : The dynamic growth of Indian Pharma Industry, and the recommendations of four major Pharma associations made the Ministry of Commerce & Industry to realize the need for separate export promotion council. Accordingly, Pharmaceuticals Export Promotion Council (PHARMEXCIL) has been set up on 12.5.2004. It issues RCMC, organize Trade delegations/Buyer-Seller Meetings abroad, Organize Reverse Buyer-Seller Meetings in India, Assist members to get their MDA/MAI claims refunded from Govt. of India, Issue of Certificate of Origin, Organizing periodical Seminars/Interactive meetings on exports related issues, Make suggestions to Govt. of India on policy issues relating to Pharma exports, Make representations to Govt. of India and other agencies in India and abroad to get amicable solutions for the common problems of the industry.

(13) Indian Oil Seeds & Produce Exporters Association : Indian Oilseed and Produce Export Promotion Council (IOPEPC) is concerned with the promotion of various Oilseeds and Oils. Formerly known as IOPEA, it was formed on 23 rd June 1956, at a preliminary meeting held in Bombay under the Presidentship of late Shri Lalji Mehrotra, former President of Federation of Indian Chambers of Commerce and Industry (FICCI) and India's one time ambassador to Myanmar and Japan. The formation of IOPEA was, in fact, the first organized effort to promote and protect the interests of India 's export trade in commodities like Oilseeds, Vegetable Oils and Oilcakes in a collective and concerted manner through a representative body. With subsequent setting up of sectoral Associations for different oilcakes and extraction cakes, IOPEPC concentrated it's attention and activities mainly on productivity and export of oilseeds and vegetable oils. IOPEPC is thus the pioneer body for oilseeds and oils in the country

(14) Services Export Promotion Council : Ministry of Commerce and Industry, Government of India, with a view to give proper direction, guidance and encouragement to the Services Sector, has set up an exclusive Export Promotion Council for Services in the name of Services Export Promotion Council (SEPC). SEPC was registered under the Societies Registration Act in November, 2006. DGFT, vide Gazette Notification dated 5/3/ 2007, included SEPC in the list of the recognised Export Promotion Councils. SEPC has been mandated to promote export of services in the following sectors:-

1	Healthcare services including services by nurses, physiotherapist and paramedical personnel	8	Environmental Services
2	Educational Services	9	Maritime Transport Services
3	Entertainment services including Audio-visual services	10	Advertising Services
4	Consultancy Services	11	Marketing Research and Public Opinion Polling Services/Management Services
5	Architectural Services and related services	12	Printing & Publishing Services
6	Distribution Services	13	Legal Services
7	Accounting/Auditing and Book Keeping Services	14	Hotel and Tourism related services

OTHER ORGANISATIONS UNDER MINISTRY OF COMMERCE

Federation of Indian Export Organisations

The Federation of Indian Export Organizations set up in 1965, is an Apex body registered under the Societies Registrations Act XXI of 1860, of various export promotion organizations and institutions with its major regional offices at Delhi, Mumbai, Chennai and Kolkata. The main objective of FIEO is to render an integrated package of services to various organizations connected with export promotion. It provides the content, direction and thrust to India's global export effort. It also functions as a primary servicing agency to provide integrated assistance to its members comprising professional exporting firms holding recognition status granted by the Government, consultancy firms and service providers. The Federation organizes seminars and arranges participation in various exhibitions in India and abroad. It also brings out 'FIEO News', for creating awareness amongst its member exporters and importers.

Indian Council of Arbitration, New Delhi

The Indian Council of Arbitration, India's premier Arbitral Institution, is a Society registered under the Societies Registration Act, 1860 operating on no profit basis, with its head office in New Delhi and eight branches with a pan India network. The organization originally established in 1965 promotes and administers the use of Alternative Dispute Resolution mechanisms in commercial disputes, thereby expediting dispute resolution and encouraging greater domestic and international commerce. The main objectives of the Council are to promote the knowledge and use of arbitration and provide arbitration facilities for amicable and quick settlement of commercial disputes with a view to maintaining the smooth flow of trade, particularly export trade on a sustained and enduring basis.

Indian Diamond Institute, Surat

With the objective of enhancing the quality, design and global competitiveness of the Indian Jewellery, the Indian Diamond Institute was established as a Society in 1978 with its office located at Surat. The Institute is sponsored by the Department of Commerce and patronized by the Gems and Jewellery Export Promotion Council (GJEPC). The Institute conducts various diploma and other courses related to diamond trade and industry. The three year diploma course on Diamond, Gem & Jewellery Design & Manufacture conducted by IDI has been accredited by All India Council for Technical Education (AICTE). The Institute also has certification services for diamonds, coloured stones and gold jewellery. IDI has a Gem Testing Lab (GTL), which is recognized by Government of India as an approved Diamond Grading / Certification Institution for cut and polished diamonds up to weight of 0.25 carat. The Institute has been recognized world over as a Diamond Certification and Grading

Laboratory. The Laboratory services provided by IDI are ISO 9001:2000 quality compliant. The Institute also has Sardar Vallabhbhai Patel Centre of Jewellery Design and Manufacture (SVJDM) which offers advanced courses in Jewellery Design and Manufacture.

Footwear Design & Development Institute (FDDI)

Footwear Design and Development Institute was established in the year 1986 as a Society under the Societies Registration Act, 1860 with an objective to train the professional manpower for footwear industry. The Institute is an ISO:9001 and ISO:14001 certified Institute, which conducts wide range of long term and short term programmes in the area of Retail Management, Fashion, Footwear Merchandising, Marketing, Creative Design & CAD/CAM and Leather Goods & Accessories Design, etc. The Institute, having Pan-India presence with seven well designed campuses at Noida, Fusatganj, Chennai, Kolkata, Rohtak, and Chhindwara & Jodhpur is providing trained human resource to the industry besides the upcoming campus at Guna. Crossing the national boundaries, the Institute is providing consultancy and training to the South Asian Association for Regional Cooperation (SAARC) countries besides African countries in the area of footwear design, technology and management.

National Centre for Trade Information

National Centre for Trade Information was set up in 1995 with a view to create an institutional mechanism for collection and dissemination of trade data and improving information services to the business community, especially small and medium enterprises. NCTI is a Government of India recognized Trade Point in India under the Trade Efficiency Programme of United Nations Conference on Trade & Development (UNCTAD). NCTI is the Operational Trade Point in India and is also the recognized Focal Point of Trade Analysis and Information System (TRAINS) of UNCTAD Trade Point Development Centre (UNTPDC). NCTI is promoted by India Trade Promotion Organization (ITPO) and National Informatics Centre (NIC).

Price Stabilization Fund Trust

The Price Stabilization Fund (PSF) Scheme was launched by Government of India in April 2003 against the backdrop of decline in international and domestic prices of tea, coffee, rubber, and tobacco causing distress to primary growers. The growers of these commodities were particularly affected due to substantial reduction in unit value realization for these crops, at times falling below their cost of production. The objective of the Scheme is to safeguard the interests of the growers of these commodities and provide financial relief when prices fall below a specified level without resorting to the practice of procurement operations by the Government agencies. The Scheme is being operationalized through the Price Stabilization Fund Trust. As on 31 October 2009, the PSF Corpus Fund consists of Rs.435.19 crore, out of which Rs.432.88 crore has been contributed by Government of India and Rs.2.31 crore by growers by way of entry fee.

A Personal Accident Insurance Scheme is also under implementation by PSFT through National Insurance Corporation Ltd., which provides insurance cover to the growers in the sectors of tea, coffee, rubber, tobacco and spices (chillies, cardamom, ginger, turmeric and pepper) having plantations up to 4 hectares. The Scheme also covers all plantation workers working on these plantations regardless of the size of holdings. The insurance cover is up to Rs. 1.00 lakh per person. The premium of Rs.17/- is shared between the beneficiary and the PSF Trust in the ratio 50:50. The target coverage is 57.17 lakh growers and workers.

GS1-India

GS1 India is a not-for-profit standards body promoted by the Ministry of Commerce (GOI) and Indian Industry to spread awareness and provide guidance on adoption of global standards in Supply Chain Management by Indian Industry for the benefit of consumers, Industry, Govt. etc.

GS1 India is the only organisation in India authorised to issue company prefix numbers for use in barcodes, RFID tags etc. for unique, unambiguous and universal identification of products, cartons, containers etc. GS1

standards find wide application in Supply Chains across sectors for unique-yet-universal product, consignment and entity identification, EDI (Electronic Data Interchange), product data synchronisation etc. GS1 standards are the dc-facto global standards in identification of consumer products in Retail. GS1 India is an affiliate of GS1 Global Office, twin headquartered at Brussels (Belgium) and Lawrenceville, New Jersey (U.S.A.), which oversees operations of a network of over 100 GS1 organisations across the world.

ADVISORY BODIES

Board of Trade (BOT)

The Board of Trade was set up on 5th May, 1989 with a view to provide an effective mechanism to maintain continuous dialogue with trade and industry in respect of major developments in the field of International Trade. The Board was reconstituted on 16th July, 2009 under the Chairmanship of Commerce & Industry Minister vide order No.01/94/180/438/AM05/BOT/PC-V. The Board, inter-alia, advises the Government on policy measures connected with the Foreign Trade Policy in order to achieve the objectives of boosting India's exports .

Terms of reference of the Board of Trade

- To advise the Government on Policy measures for preparation and implementation of both short & long term plans for increasing exports in the light of emerging national and international economic scenario;
- To review export performance of various sectors, identify constraints and suggest industry specific measures to optimize export earnings;
- To examine the existing institutional framework for imports and exports and suggest practical measures for further streamlining to achieve the desired objectives; and
- To review the policy instruments and procedures for imports and exports and suggest steps to rationalize and channelize such schemes for optimum use.

Inter State Trade Council

The Inter State Trade Council was set up on 24th June, 2005 with a view to serve as a mechanism for institutionalized dialogue between the Union and the States in matters relating to trade facilitation and to create a framework for making States partners in India's export effort. The Council is represented by Chief Ministers of the States or State Cabinet Ministers nominated by Chief Ministers, Lt. Governors or Administrators of the Union Territories or their nominees, Secretaries of the Departments of Commerce, Revenue, Industrial Policy & Promotion, Agriculture & Cooperation, Shipping, Road Transport & Highways, Ministries of External Affairs, Power and Chairman, Railway Board. It also co-opts the Chairman-cum-Managing Director of Export Credit Guarantee Corporation, Managing Director of EXIM Bank, Deputy Governor of Reserve Bank of India, Chairman of Agricultural and Processed Food Products Export Development Authority, Chairman of Marine Products Export Development Authority and presidents of CII, FICCI, FIEO, ASSOCHAM and Export Promotion Council for EOUs/ SEZs.

ATTACHED AND SUBORDINATE OFFICES

Directorate General of Foreign Trade (DGFT)

This Directorate, with headquarters at New Delhi, is headed by the Director General. Keeping in line with liberalization and globalization and the overall objective of increasing of exports, DGFT is assigned the role of a "facilitator". It is responsible for implementing the Foreign Trade Policy with the main objective of promoting India's exports. The DGFT also issues licenses to exporters and monitors their corresponding obligations through a network of 35 Regional Offices. All DGFT offices provide facilitation to exporters in regard to developments in the area of international trade, i.e. WTO agreements, Rules of Origin and Sanitary and Phytosanitary Measures

(SPS) requirements, Anti-Dumping issues, etc. to help the exporters to strategize their import and export decisions in an internationally dynamic environment.

Directorate General of Supplies and Disposal (DGS&D)

The DGS&D, with headquarters at New Delhi, is headed by the Director General. It functions as the executive arm of the Supply Division of the Department of Commerce for conclusion of Rate Contracts for common user items, procurement of stores, inspection of stores, shipment and clearance of imported stores/ cargo. It has three Regional Offices located at Chennai, Mumbai and Kolkata. The functions of DGS&D are carried out through its functional wings and supporting service wings. The functional wings are the Supply Wing and the Quality Assurance Wing. The supporting service wings include Administration, Vigilance, Complaints and Public Relations, Planning and Co-ordination, Internal Work Study, Management Information Services, Litigation, etc.

The Supply Wing has commodity-wise Purchase Directorates such as Information Technology, Electrical Stores, Mechanical Engineering, Automobiles, Steel & Cement, Structural Engineering, Hardware, Workshop & Machine Tools, Wool & Leather, Paper & Paper Products, Oil & Chemicals. The handling of commodity-wise work facilitates maintenance of data bank on prices, vendors, specifications, market trends, etc. The Quality Assurance Wing has 26 offices/sub-centres (including headquarters) spread all over the country.

Directorate General of Anti-Dumping & Allied Duties (DGAD)

The Directorate General of Anti-Dumping & Allied Duties was constituted in April, 1998 and is headed by the Designated Authority of the level of Additional Secretary to the Government of India who is assisted by a Joint Secretary, Adviser (Cost) and Additional Economic Adviser. Besides, there are twelve Investigating and Costing Officers to conduct investigations. The Directorate is responsible for carrying out investigations and to recommend, where required, under Customs Tariff Act, the amount of anti-dumping duty/ countervailing duty on the identified articles which would be adequate to remove injury to the domestic industry.

(B) Subordinate Offices

Directorate General of Commercial Intelligence and Statistics (DGCI&S)

The Directorate General of Commercial Intelligence & Statistics (DGCI&S) is the premier organization of Govt. of India for collection, compilation and dissemination of India's Trade Statistics and Commercial Information. This Directorate, with its office located at Kolkata, is headed by the Director General. It is entrusted with the work of collecting, compiling and publishing/disseminating trade statistics and various types of commercial information required by the policy makers, researchers, importers, exporters, traders as well as overseas buyers. DGCI&S collects the basic data from different customs formations in the form of DTR (Daily Trade Return) and then processes and compiles it using state-of-the-art technology.

The foreign trade data generated by the Directorate are disseminated through (i) Monthly Press Release brought out every month by the Ministry of Commerce and Industry, (ii) Monthly Foreign Trade Statistics of India by Principal Commodities & Countries, (iii) Monthly Statistics of Foreign Trade of India (Import & Export), and (iv) Quarterly Statistics of Foreign Trade of India by Countries. It also brings out an Assessment Report on India's Foreign Trade by Air, every year. As far as ancillary statistics is concerned, DGCI&S also compiles and publishes on regular basis the Inland Trade Statistics covering Inter-State Movements of Goods by Rail, River and Air, Statistics on India's Customs and Excise Revenue Collections (according to the tariff heads), Shipping Statistics, Inland Coastal Trade Statistics and Selected Statistics of Foreign Trade of India.

DGCI&S foreign data processing system is built on ORACLE database and SUN ULTRA E-450 system. Its computer system is having networking facilities both in-house and with outside world. There are two SUN M4000 database Servers and two SUN T2000 Application Servers with adequate storage and tape drives.

A dedicated 512 kbps leased line installed is being used to receive the DTR data online from computerized Customs houses. Along with this, some direct Broadband lines are also available to support the lease line.

The Directorate brings out a number of publications on, inter alia, inland and coastal trade statistics, revenue statistics, shipping & air cargo statistics etc, which are utilized by the Government Departments as well as by trading communities and researchers. India Trade Journal, a weekly publication, is the premier publication of DGCI&S. The dynamic pages of the DGCI&S website www.dgciskol.nic.in are mainly for online data transmission and provide access to data under PIS (Priced Information Service System).

Offices of Development Commissioner of Special Economic Zones (SEZs)

The main objectives of the SEZ Scheme are generation of additional economic activity, promotion of exports of goods and services, promotion of investment from domestic and foreign sources, creation of employment opportunities along with the development of infrastructure facilities. All laws of India are applicable in SEZs unless specifically exempted as per the SEZ Act/ Rules. Each Zone is headed by a Development Commissioner and is administered as per the SEZ Act, 2005 and SEZ Rules, 2006. There are currently eight Development Commissioners of SEZs. Units may be set up in the SEZ for manufacturing, trading or for service activity. The units in the SEZ have to be net foreign exchange earners but they are not subjected to any predetermined value addition or minimum export performance requirements. Sales in the Domestic Tariff Area from the SEZ units are treated as if the goods are being imported and are subject to payment of applicable customs duties.

Pay and Accounts Office (Supply)

The payment and accounting functions of Supply Division, including those of DGS&D, are performed by the Chief Controller of Accounts (CCA) under the Departmentalized Accounting System. Payment to suppliers across the country is made through this organization.

Pay and Accounts Office (Commerce & Textiles)

The Pay and Accounts Office, common to both the Department of Commerce and the Ministry of Textiles, is responsible for the payment of claims, accounting of transactions and other related matters through the four Departmental Pay & Accounts Offices in Delhi, two in Mumbai, two in Kolkata and two in Chennai. These Departmental Pay and Accounts Offices are controlled by the Principal Accounts Office at Delhi with the Chief Controller of Accounts (CCA) as the Head of the Department of the Accounts Wing.

EXIM BANK OF INDIA

Export-Import Bank of India is the premier export finance institution of the country, set up in 1982 under the Export-Import Bank of India Act 1981 with the objective for providing financial assistance to exporters and importers, and for functioning as the principal financial institution for coordinating the working of institutions engaged in financing export and import of goods and services with a view to promoting the country's international trade. Government of India launched the institution with a mandate, not just to enhance exports from India, but to integrate the country's foreign trade and investment with the overall economic growth. Since its inception, Exim Bank of India has been both a catalyst and a key player in the promotion of cross border trade and investment. Commencing operations as a purveyor of export credit, like other Export Credit Agencies in the world, Exim Bank of India has, over the period, evolved into an institution that plays a major role in partnering Indian industries, particularly the Small and Medium Enterprises, in their globalisation efforts, through a wide range of products and services offered at all stages of the business cycle, starting from import of technology and export product development to export production, export marketing, pre-shipment and post-shipment and overseas investment.

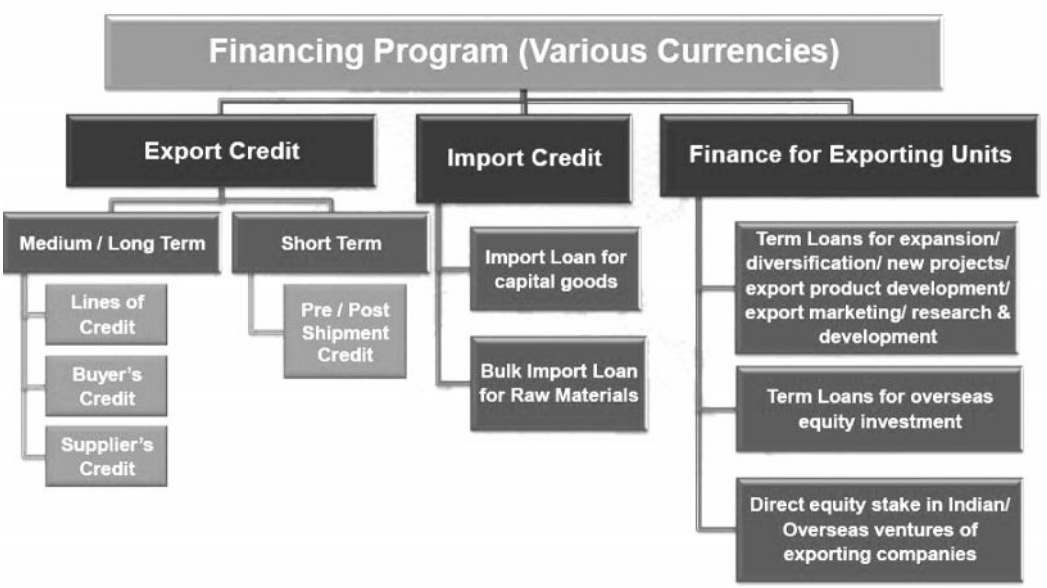
The bank provides a variety of products and services at all stages of export.



Some of the initiatives taken by the bank are as follows –

- Exim Bank of India has been the prime mover in encouraging project exports from India. The Bank provides Indian project exporters with a comprehensive range of services to enhance the prospect of their securing export contracts, particularly those funded by Multilateral Funding Agencies like the World Bank, Asian Development Bank, African Development Bank and European Bank for Reconstruction and Development.
- The Bank extends lines of credit to overseas financial institutions, foreign governments and their agencies, enabling them to finance imports of goods and services from India on deferred credit terms. Exim Bank's lines of Credit obviate credit risks for Indian exporters and are of particular relevance to SME exporters.
- The Bank's Overseas Investment Finance programme offers a variety of facilities for Indian investments and acquisitions overseas. The facilities include loan to Indian companies for equity participation in overseas ventures, direct equity participation by Exim Bank in the overseas venture and non-funded facilities such as letters of credit and guarantees to facilitate local borrowings by the overseas venture.
- The Bank provides financial assistance by way of term loans in Indian rupees/foreign currencies for setting up new production facility, expansion/modernization/upgradation of existing facilities and for acquisition of production equipment/technology. Such facilities particularly help export oriented Small and Medium Enterprises for creation of export capabilities and enhancement of international competitiveness.
- Under its Export Marketing Finance programme, Exim Bank supports Small and Medium Enterprises in their export marketing efforts including financing the soft expenditure relating to implementation of strategic and systematic export market development plans.
- The Bank has launched the Rural Initiatives Programme with the objective of linking Indian rural industry to the global market. The programme is intended to benefit rural poor through creation of export capability in rural enterprises.
- In order to assist the Small and Medium Enterprises, the Bank has put in place the Export Marketing Services (EMS) Programme. Through EMS, the Bank seeks to establish, on best efforts basis, SME sector products in overseas markets, starting from identification of prospective business partners to facilitating placement of final orders. The service is provided on success fee basis.
- Exim Bank supplements its financing programmes with a wide range of value-added information, advisory and support services, which enable exporters to evaluate international risks, exploit export opportunities and improve competitiveness, thereby helping them in their globalisation efforts

Various financing programmes of Exim Bank are given in the diagram below:



LESSON ROUND UP

- The short term objective of Foreign Trade policy is to arrest and reverse the declining trend of exports and to provide additional support especially to those sectors which have been hit badly by recession in the developed world. By 2014, it expects to double India's exports of goods and services. The long term policy objective for the Government is to double India's share in global trade by 2020.
- In exercise of powers conferred by Section 5 of the Foreign Trade (Development & Regulation) Act, 1992 (No.22 of 1992) the Central Government notified the Foreign Trade Policy, 2009-2014.The Foreign Trade Policy 2009-2014 (FTP), incorporating provisions relating to export and import of goods and services.
- The Foreign Trade Policy prohibits export or import by any person without an IEC number unless specifically exempted. An IEC number is granted on application by competent authority in accordance with specified procedure.
- Under MAI scheme, financial assistance is provided for export promotion activities on focus country, focus product basis. Financial assistance is also available for Export Promotion Councils (EPCs), Industry and Trade Associations (ITAs), Agencies of State Government, Indian Commercial Missions (ICMs) abroad and other national level institutions/eligible entities.
- Under MDA Scheme, financial assistance is provided for a range of export promotion activities implemented by Export Promotion Councils and Trade Promotion Organizations on the basis of approved annual action plans.
- Merchant as well as Manufacturer Exporters, Service Providers, Export Oriented Units (EOUs) and Units located in Special Economic Zones (SEZs), Agri Export Zones (AEZs), Electronic Hardware Technology Parks (EHTPs), Software Technology Parks (STPs) and Bio- Technology Parks (BTPs) shall be eligible for status of export and trading houses.

- Objective of focus market scheme is to offset high freight cost and other externalities to select international markets with a view to enhance India's export competitiveness in these countries. Exporters of all products to notified countries shall be entitled for Duty Credit Scrip.
- Objective of focus product scheme is to incentivise export of such products which have high export intensity/employment potential, so as to offset infrastructure inefficiencies and other associated costs involved in marketing of these products.
- Units undertaking to export their entire production of goods and services (except permissible sales in DTA), may be set up under the Export Oriented Unit (EOU) Scheme, Electronics Hardware Technology Park (EHTP) Scheme, Software Technology Park (STP) Scheme or Bio-Technology Park (BTP) Scheme for manufacture of goods, including repair, re-making, reconditioning, reengineering and rendering of services.
- Duty Exemption Schemes consist of (a) Advance Authorisation scheme and (b) Duty Free Import Authorisation (DFIA) scheme.
- The main objectives of the EOU scheme is to increase exports, earn foreign exchange to the country, transfer of latest technologies stimulate direct foreign investment and to generate additional employment.
- The SEZ Act 2005 envisages key role for the State Governments in Export Promotion and creation of related infrastructure. Any individual, co-operative society, company or partnership firm can file an application for setting up of Special Economic Zone.
- The Free Trade and Warehousing Zones (FTWZ) is a special category of Special Economic Zone and is governed by the provisions of the SEZ Act and the Rules.
- The organisational structure for promotion of exports includes a number of councils and organisations set up during the post- independence period.
- The Department of Commerce, Government of India is the most important organ concerned with the regulation, development and promotion of India's international trade and commerce through formulation of appropriate international trade & commercial policy and implementation of the various provisions thereof.
- The Export Promotion Councils are Non-profit, Autonomous and Professional Bodies registered under the Indian Companies Act or the Societies Registration Act, as the case may be.

SELF TEST QUESTIONS

1. What are the objectives of foreign trade policy?
2. Write a brief about the Foreign trade policy 2009 -14.
3. Specify the authority responsible for the administration and execution of the FTP?
4. Distinguish between Market Access Scheme and Market development Assistance.
5. Explain the role of ministry of commerce in promotion of exports in India.
6. What is Export promotion Council? Write in brief about various EPCs in India.
7. Write about the privileges given to export and trading houses.
8. Explain the features of SEZs. Also point out the facilities and benefits given to SEZs.
9. What are different commodity boards in India? Explain their role in promotion of specific commodities in India.

10. Write short notes on:
    - Board of Trade
    - Star Export House
    - Export oriented units
    - EPCG scheme
    - Free trade and warehousing zones

Lesson 5
Foreign Trade Policy and Procedures Part II – Export Management

LESSON OUTLINE

- Concept of Export
- Reasons for export
- Planning for export
- Product selection
- Market selection
- Registration of exporters
- Importer Exporter Code Number
- Export License
- Inquiry and Offer for Exports
- Sample Exports
- Export Pricing
- INCOTerms
- Export Documents
- Methods of payment/ payment terms
- Export Financing
  - Pre Shipment Finance
  - Post Shipment Finance
- Factoring and forfaiting
- Quality control on exports
- Packing and Labelling of Goods
- Central Excise Clearance procedure for Export
- Customs Procedure for Export
- Export Risk Management
- LESSON ROUND UP
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

No doubt that in the age of globalisation and liberalisations, export has became one of the most lucrative business in India. Government of India is also supporting exporters through various incentives and schemes to promote Indian export for meeting the much needed requirements for importing modern technology and adopting new technology from MNCs through joint ventures and collaborations.

Export of commercial quantities of goods normally requires involvement of the customs authorities in both the country of export and the country of import. Exports are subject to legal restrictions applied by the country of export. Export in itself is a very wide concept and lot of preparations is required by an exporter before starting an export business. The exporting activity requires several commercial and regulatory procedures.

In this chapter regulatory procedures and documentation for exports have been discussed in detail. We will also study about methods of financing exports, central excise and customs procedure for export in India and finally export risk management will also be discussed.

Export Management means planning, organising, coordinating and control export efforts or activities to achieve desired export objectives smoothly and with continuance.

CONCEPT OF EXPORT

The term export derives from the conceptual meaning as to ship the goods and services out of the port of a country. The seller of such goods and services is referred to as an "exporter" who is based in the country of export whereas the overseas based buyer is referred to as an "importer". In International Trade, "exports" refers to selling goods and services produced in the home country to other markets. In very simple terms, export may be defined as the selling of goods to a foreign country. However, As per Section 2 (e) of the India Foreign Trade (Development & Regulations) Act (1992), the term export may be defined as 'an act of taking out of India any goods by land, sea or air and with proper transaction of money".

Exporting a product is a profitable method that helps to expand the business and reduces the dependence in the local market. It also provides new ideas, management practices, marketing techniques, and ways of competing, which is not possible in the domestic market. Even as an owner of a domestic market, an individual businessman should think about exporting. Research shows that, on average, exporting companies are more profitable than their non-exporting counterparts. A key success factor in starting any export company is clear understanding and detail knowledge of products to be exported. In order to be a successful in exporting one must fully research its foreign market rather than trying every market. The exporter should approach a market on a priority basis. There are specific laws dealing with International trade and foreign business, it is imperative that exporter familiarize himself with state, federal, and international laws before starting export business. Price is also an important factor. So, before starting an export business an exporter must consider and fix the price offered to the buyers.

REASONS FOR EXPORT

There are many good reasons for exporting. Some of the motives of export are given below:

- The first and the primary reason for export is to earn foreign exchange. The foreign exchange not only brings profit for the exporter but also improves the economic condition of the country.
- Secondly, companies that export their goods are believed to be more reliable than their counterpart domestic companies assuming that exporting company has survived the test in meeting international standards.
- Thirdly, free exchange of ideas and cultural knowledge opens up immense business and trade opportunities for a company.
- Fourthly, as one starts visiting customers to sell one's goods, he has an opportunity to start exploring for newer customers, state-of-the-art machines and vendors in foreign lands.
- Fifthly, by exporting goods, an exporter also becomes safe from offset lack of demand for seasonal products.
- Lastly, international trade keeps an exporter more competitive and less vulnerable to the market as the exporter may have a business boom in one area while simultaneously witnessing a bust in a different area.

PLANNING FOR EXPORT

The organisation should plan well before exporting as to what product to be exported, where to be exported etc. The organisation should also evaluate the export potential of a company. The main objective of a typical export plan should be to identify:

- The objectives of exporting

- Lists of activities to undertake to achieve those objectives.
- Mechanism for review and
- Activities to help focus on goals.

For a proper export planning following questions need to answered:

- Which products are selected for export development?
- What modifications, if any, must be made to adapt them for overseas markets?
- Which countries are targeted for sales development?
- In each country, what is the basic customer profile?
- What marketing and distribution channels should be used to reach customers?
- What special challenges pertain to each market (competition, cultural differences, import controls, etc.), and what strategy will be used to address them?
- How will the product's export sale price be determined?
- What specific operational steps must be taken and when?
- What will be the time frame for implementing each element of the plan?
- What personnel and company resources will be dedicated to exporting?
- What will be the cost in time and money for each element?
- How will results be evaluated and used to modify the plan?

PRODUCT SELECTION

The product to be exported should be selected keeping in mind following factors-

- The product should be manufactured or sourced with consistent standard quality, comparable to your competitors. ISO or equivalent certification helps in selling the product in the international market.
- The manufacturing of the product should not be dependent upon the monopoly of one or few suppliers. Timely supply is a key success factor in export business.
- The price of the exported product should not fluctuate very often - threatening profitability to the export business.
- The government policies related to the export of a particular product should be checked.
- The various government incentive schemes and tax exemption like duty drawback and DEPB should be studied.
- Import regulation in overseas markets, specially tariff and non-tariff barriers should be checked. Though a major tariff barriers has been abolished - there are still same tariff and non-tariff barriers. If the product attracts higher duty in target country - demand of the product will be low.
- Registration/Special provision for the products in importing country should be known. This is specially applicable for processed food and beverages, drugs and chemicals.
- Seasonal vagaries of selected products as some products sell in summer, while others in winter should be indentified. Festive season is also important factor, for example certain products are more saleable only during Christmas.

- Special packaging and labelling requirements of perishable products like processed food and dairy products should be known.
- Special measures are required for transportation of certain products, which may be bulky or fragile or hazardous or perishable which must be indentified.

MARKET SELECTION

Foreign Market for exports should be selected after research and due consideration. The steps to be followed are-

***Step 1*:** Gather Information on a Broad Range of Markets depending upon the products or services to be exported, which includes:

- The demand for product/service.
- The size of the potential audience.
- Whether the target audience can afford product.
- What the regulatory issues are that impact on exports of product.
- Ease of access to this market – proximity/freight.
- Are there appropriate distribution channels for product/service?
- The environment for doing business – language, culture, politics etc.
- Is it financially viable to export to selected market?

***Step 2*:** From the results of the first stage, narrow your selection down to three to five markets and undertake some in-depth research relating specifically to your product. While doing so, some of the questions that may arise at this stage are:

- What similar products are in the marketplace (including products that may not be similar but are used to achieve the same goal, e.g. the product in our sample matrix at the end of this document is a hair removal cream. As well as undertaking competitor research on other hair removal creams, we would also need to consider other products that are used for hair removal, i.e. razors, electrolysis, wax).
- What is your point of difference? What makes your product unique? What are the key selling points for your product?
- How do people obtain/use these products?
- Who provides them?
- Are they imported? If so from which countries?
- Is there a local manufacturer or provider?
- Who would your major competitors be? What are the key brands or trade names?
- What is the market's structure and shape?
- What is the market's size?
- Are there any niche markets, and if so how big are they?
- Who are the major importers/ stockists / distributors / agencies or suppliers?
- What are the other ways to obtain sales/representation?
- What are the prices or fees in different parts of the market?

- What are the mark-ups at different distribution levels?
- What are the import regulations, duties or taxes, including compliance and professional registrations if these apply?
- How will you promote your product or service if there is a lot of competition?
- Are there any significant trade fairs, professional gathers or other events where you can promote your product or service?
- Packaging – do you need to change metric measures to imperial, do you need to list ingredients?
- Will you need to translate promotional material and packaging?
- Is your branding – colours, imagery etc., culturally acceptable?

After selecting the market, the organisations plan how to export in those markets. Various methods could be like direct selling, indirect selling and promotion, seeking alliances or agreements etc as discussed in chapter one of this study.

GENERAL PROVISIONS REGARDING IMPORTS AND EXPORTS

Exports and Imports have been made free in India, except where regulated by Foreign Trade Policy or any other law for the time being in force. The item wise export and import policy would however be, as specified in Indian Trade Classification (Harmonised System) "ITC(HS)" notified by Director General of Foreign Trade, as amended from time to time. Every exporter or importer is required to comply with the provisions of Foreign Trade (Development & Regulation) Act, the rules and orders made there-under, Foreign Trade Policy and terms and conditions of any authorisation granted to him. All imported goods have also been made subject to domestic laws, rules, orders, regulations, technical specifications, environmental and safety norms as applicable to domestically produced goods. The import or export of rough diamonds is not permitted unless accompanied by Kimberley Process (KP) Certificate as specified by Gem & Jewellery Export Promotion Council (GJEPC).

REGISTRATION OF EXPORTERS

Once all the research and analysis is done by the exporting organisation, its time to get registered with the various government authorities before it starts to export.

Registration with Reserve Bank of India (RBI)

Prior to 1997, it was necessary for every first time exporter to obtain IEC number from Reserve Bank of India (RBI) before engaging in any kind of export operations. But now this is being done by DGFT.

Registration with Director General of Foreign Trade (DGFT)

For every first time exporter, it is necessary to get registered with the DGFT (Director General of Foreign Trade), Ministry of Commerce, Government of India. DGFT provide exporter a unique IEC Number. IEC Number is a ten digits code required for the purpose of export as well as import. Detail procedure of obtaining IEC Code is given in following pages.

Registration with Export Promotion Council

Registered under the Indian Company Act, Export Promotion Councils or EPC is a non-profit organisation for the promotion of various goods exported from India in international market. EPC works in close association with the Ministry of Commerce and Industry, Government of India and act as a platform for interaction between the exporting community and the government. So, it becomes important for an exporter to obtain a **Registration cum Membership Certificate (RCMC)** from the EPC. An application for registration should be accompanied by a self certified copy of the IEC number. Membership fee should be paid in the form of cheque or draft after

ascertaining the amount from the concerned EPC. The RCMC certificate is valid from 1st April of the licensing year in which it was issued and shall be valid for five years ending 31st March of the licensing year, unless otherwise specified.

Registration with Commodity Boards

Commodity Board is registered agency designated by the Ministry of Commerce, Government of India for purposes of export-promotion and has offices in India and abroad. At present, there are five statutory Commodity Boards under the Department of Commerce. These Boards are responsible for production, development and export of tea, coffee, rubber, spices and tobacco.

Registration with Income Tax Authorities

Goods exported out of the country are eligible for exemption from both Value Added Tax and Central Sales Tax. So, to get the benefit of tax exemption it is important for an exporter to get registered with the Tax Authorities.

IMPORTER EXPORTER CODE NUMBER (IEC)

IEC Code is unique 10 digit code issued by DGFT – Director General of Foreign Trade, Ministry of Commerce, and Government of India to Indian Companies. To import or export in India, IEC Code is mandatory. No person or entity shall make any Import or Export without IEC Code Number. Directorate General of Foreign Trade (DGFT) issued a Policy Circular No.15 (RE-2006)/2004-2009 Date: 27th July, 2006) for New System for issuance of Importer-Exporter Code Number. Eligibility condition and Legal Provisions are given for IEC Code Number Application in Foreign Trade (Regulation) Rules, 1993 Ministry of Commerce, and Notification No. GSR 791 (E), dated 30-12-1993.

Application for Grant of IEC Number

An application for grant of IEC number shall be made by the Registered/Head Office of the applicant and apply to the nearest Regional Authority of Directorate General Foreign Trade, where the Registered office in case of company and Head office in case of others, falls in the ‘Aayaat Niryaat Form - ANF2A’ and shall be accompanied by documents prescribed therein. In case of STPI/ EHTP/ BTP units, the Regional Offices of the DGFT having jurisdiction over the district in which the Registered/ Head Office of the STPI unit is located and shall issue or amend the IECs. Only one IEC would be issued against a single PAN number. Any proprietor can have only one IEC number and in case there are more than one IECs allotted to a proprietor, the same may be surrendered to the Regional Office for cancellation.

IEC Code Online Application Form

The application can be download Form in PDF or Word. This is called "Aayaat Niryaat Form - ANF2A". Along with IEC Code Number Application Form it is necessary to submit Appendix-18B Attested by Applicant’s Banker in his letter head with two passport size photo).

List of Regional Authorities of DGFT and the Corresponding Office of Reserve Bank of India, Exchange Control Department: The list of Foreign Exchange Control Department of the RBI is given in Appendix-18D.

Validity of IEC Code No

An IEC number allotted to an applicant shall be valid for all its branches/divisions/units/factories as indicated in the format of IEC given in Appendix- 18B.

Duplicate Copy of IEC Number

Where an IEC Number is lost or misplaced, the issuing authority may consider requests for grant of a duplicate copy of IEC number, if accompanied by an affidavit.

Surrender of IEC Number

If an IEC holder does not wish to operate the allotted IEC number, he may surrender the same by informing the issuing authority. On receipt of such intimation, the issuing authority shall immediately cancel the same and electronically transmit it to DGFT for onward transmission to the Customs and Regional Authorities.

Application Fee For IEC Code Number

Application Fee is Rs. 250 payable in favour of "Zonal Joint Director General of Foreign Trade" through bank order or demand draft or EFT (Electronic Fund Transfer by Nominated Bank by DGFT Like HDFC Bank, ICICI Bank, State Bank of India, UTI Bank, Punjab National Bank, Central Bank etc). The application fee can also be deposited by TR6 Challan with Duplicate Copy in any branch of Central Bank of India and TR6 Challan need to be submited along with IEC Code Application.

Territorial Jurisdiction of Regional Authorities

Every application, unless otherwise specified, shall be submitted to the Regional Authority of Directorate General Foreign Trade, as per the territorial jurisdiction of the Regional authorities indicated in Policy and Handbook of Procedure Volume-I.

Filing of Application

Application can be filed online in DGFT website, details of online links are given at the end of this topic. Every application for an Import/Export licence/ certificate/ authorisation/ permission or any other purpose should be complete in all respects as required under the relevant provisions of the Policy/Procedures and shall be signed by the applicant. An incomplete application is liable to be rejected giving specific reason for rejection. However in case of manual applications, the applicant would furnish a soft copy of the application in MS word format.

Profile of Importer/ Exporter

Each Importer/Exporter shall be required to file importer/ exporter profile once with the Regional Authority in Part 1 of 'Aayaat Niryaat Form - ANF2A'. Regional Authority shall enter the information furnished in Part 1 of 'Aayaat Niryaat Form ANF-2A' in their database so as to dispense with the need for asking the repetitive information. In case of any change in the information given in Part 1 of 'Aayaat Niryaat Form ANF-2A', importer/exporter shall intimate the same to the Regional Authority.

Self Addressed Stamped Envelope

The applicant shall furnish a self addressed envelope of 40 x 15 cm with postal stamp affixed on the envelope as follows for all documents required to be sent by Speed Post:

(a) Within local area	Rs. 25.00
(b) Up to 200 Kms.	Rs. 25.00
(c) Between 200 to 1000 Kms	Rs. 30.00
(d) Beyond 1000 Kms.	Rs. 50.00

Exempted categories

The following categories of importers or exporters are exempted from obtaining Importer - Exporter Code (IEC) number:

– Importers covered by clause 3 (1) [except sub-clauses (e) and (l)] and exporters covered by clause 3(2) [except sub-clauses (i) and (k)] of the Foreign Trade (Exemption from application of Rules in certain cases) Order, 1993.

- Ministries/Departments of the Central or State Government.
- Persons importing or exporting goods for personal use not connected with trade or manufacture or agriculture.
- Persons importing/exporting goods from/to Nepal provided the CIF value of a single consignment does not exceed Indian Rs.25,000.
- Persons importing/exporting goods from/to Myanmar through Indo-Myanmar border areas provided the CIF value of a single consignment does not exceed Indian Rs.25,000.

However, the exemption from obtaining Importer-Exporter Code (IEC) number shall not be applicable for the export of Special Chemicals, Organisms, Materials, Equipments and Technologies (SCOMET) as listed in Appendix- 3, Schedule 2 of the ITC(HS) except in the case of exports by category(ii) above.

Permanent IEC Number

- The following permanent IEC numbers shall be used by the categories of importers/ exporters mentioned against them for import/ export purposes.

S.No	Code Number	Categories of Importers / Exporters
1	0100000011	All Ministries / Departments of Central Government and agencies wholly or partially owned by them.
2	0100000029	All Ministries / Departments of any State Government and agencies wholly or partially owned by them.
3	0100000037	Diplomatic personnel, Counselor officers in India and officials of UNO and its specialised agencies.
4	0100000045	Indians returning from / going abroad and claiming benefit under Baggage Rules.
5	0100000053	Persons / Institutions / Hospitals importing or exporting goods for personnel use, not connected with trade or manufacture or agriculture.
6	0100000061	Persons importing / exporting goods from /to Nepal
7	0100000070	Persons importing / exporting goods from /to Myanmar through Indo-Myanmar border areas
8	0100000088	Ford Foundation
9	0100000096	Importers importing goods for display or use in fairs / exhibitions or similar events under provisions of ATA carnet This IEC number can also be used by importers importing for exhibitions/fairs as per Para 2.29 of HBPv1.
10	0100000100	Director, National Blood Group Reference Laboratory, Bombay or their authorized offices.
11	0100000126	Individuals / Charitable Institution /Registered NGOs importing goods, which have been exempted from Customs duty under Notification issued by Ministry of Finance for bonafide use by victims affected by natural calamity.
12	0100000134	Persons importing / exporting permissible goods as notified from time to time, from / to China through Gunji, Namgaya Shipkila and Nathula ports, subject to value ceilings of single consignment as given in Para 2.8(iv) above.
13	0100000169	Non-commercial imports and exports by entities who have been authorized by Reserve Bank of India.

Note: Commercial Public Sector Undertakings (PSU) who have obtained PAN will however be required to obtain Importer Exporter Code number. The permanent IEC number as mentioned above shall be used by non-commercial PSUs.

Mandatory Requirements to apply for IEC Code Number

1. Covering letter
2. Fill Part A, B & D of the application form.
3. Application must be accompanied by documents as per details given below:
   - Bank Certificate from the bank on Bank letter head as per proforma (Part B) given in the application.
     (a) In case of Proprietorship firms, please furnish
         (i) Date of Birth of individual
         (ii) Number of IECs held along with their details
     (b) In case of Companies, please furnish
         (i) Extract of Board of Resolution.
         (ii) MOA with Form 32 and ROC in case of change in Directors.
     (c) In case of others
         (i) Notorised Partnership Deed showing date of formation.
         (ii) No Objection Certificate from other partners/HUF.
   - Self certified copy of Permanent Account Number (PAN) issued by income Tax Authorities.
   - Two copies of passport size photographs of the applicant. The photograph pasted on the banker's certificate must be attested by the banker with Seal and Signature of the applicant.
4. The application must be submitted in Duplicate.
5. Each individual page of the application must be signed by the applicant.
6. Self addressed envelope stamped with Rs. 25 (Local Address) & for others Rs.30/-. These documents may be kept secured in a file cover.

Check List of Documents to apply for IEC Code

1. Covering Letter on your company's letter head for issue of new IEC Code Number.
2. Two copies of the application in prescribed format (Aayaat Niryaat Form ANF 2A) must be submitted to your regional Jt.DGFT Office.
3. Each individual page of the application has to be signed by the applicant.
4. Part 1 & Part 4 has to be filled in by all applicants. In case of applications submitted electronically.
5. No hard copies of Part 1 may be submitted. However in cases where applications are submitted otherwise, hard copy of Part 1has to be submitted.
6. Only relevant portions of Part 2 need to be filled in.
7. Rs 250.00 Bank Receipt (in duplicate)/Demand Draft/EFT details evidencing payment of application fee in terms of Appendix 21B.
8. Certificate from the Banker of the applicant firm in the format given in Appendix 18A.

9. Self certified copy of PAN issuing letter or PAN (Permanent Account Number) Card issued by Income Tax Authority.
10. Two copies of passport size photographs of the applicant duly attested by the Banker of the applicant.
11. Self addresses envelope with Rs.25/- postal stamp for delivery of IEC certificate by registered post or challan/DD of Rs.100/- for speed post.

How to submit IEC Code application

Application can be submitted in person/by Authorised Employee of the Company at the R & I counters in the office Or It can be sent by post/courier.

Processing of IEC Code Application

The application can be submitted at the counter in person at the office or it can be sent through Post/Courier. An acknowledgement in form of a receipt having File Number is generated on receipt of application. The file number is used for any correspondence/query regarding the IEC application submitted to the office. The application is then sent to IEC section where it is processed. If the application is found complete in all aspects (as per requirements prescribed) an IEC is generated, or else a deficiency letter stating the nature of deficiency is prepared and sent to the applicant. Replies are awaited in cases where deficiency letter is issued and after due compliance by the applicant the IEC is allotted.

Issue and Despatch of IEC Code

IEC allotment letter is sent through post at the registered office mentioned by the applicant in the application. Similarly deficiency letters are sent to applicant by post.

About IEC Application Status

A new option to know the file number has been introduced for all exporters who are sending their application through Post/Courier. The applicant has to input PAN number to get the file number. The applicant can know the status of the IEC application using option “Status of IEC Application” on the website of CLA.

IEC Code Number Related links

- View Your IEC Status : *http://dgft.delhi.nic.in:8100/dgft/iecprint*
- IEC Status at Custom(BIN) : *http://164.100.9.176/iecstatus.html*
- http://www.dgft.gov.in/dgftcla
- http://www.dgft.gov.in
- *http://www.icegate.gov.in*

EXPORT LICENSE

An export license is a document issued by the appropriate licensing agency after which an exporter is allowed to transport his product in a foreign market. The license is only issued after a careful review of the facts surrounding the given export transaction. Export license depends on the nature of goods to be transported as well as the destination port. So, being an exporter it is necessary to determine whether the product or good to be exported requires an export license or not.

Canalisation

Canalisation is an important feature of Export License under which certain goods can be imported only by designated agencies. For an example, an item like gold, in bulk, can be imported only by specified banks like SBI and some foreign banks or designated agencies.

Application for an Export License

To determine whether a license is needed to export a particular commercial product or service, an exporter must first classify the item by identifying what is called ITC (HS) Classifications. Export license are only issued for the goods mentioned in the Schedule 2 of ITC (HS) Classifications of Export and Import items. A proper application can be submitted to the Director General of Foreign Trade (DGFT). The Export Licensing Committee under the Chairmanship of Export Commissioner considers such applications on merits for issue of export licenses.

Exports Free unless regulated

The Director General of Foreign Trade (DGFT) from time to time specifies through a public notice according to which any goods, not included in the ITC (HS) Classifications of Export and Import items may be exported without a license. Such terms and conditions may include Minimum Export Price (MEP), registration with specified authorities, quantitative ceilings and compliance with other laws, rules, regulations

INQUIRY AND OFFER FOR EXPORTS

Export sales leads or inquiry forms are initial contacts a seller or exporter seeks in order to finalize a deal or agreement for export of goods and are considered as the first step in the entire sales process. After getting the first lead, a company should respond to that lead in a very careful manner in order to convert that opportunity into real export deal. Sales leads can be generated either through a word-of-mouth or internet research or trade show participation. As the buyer is far away and sometimes communication process can be difficult, so it's always better to make an extra effort to understand the exact need of the customer. After receiving a lead it is quite important to acknowledge the enquirer within 48 hours of receiving the enquiry either through e-mail or fax. Acknowledgement also gives an option to provide further detail about the product or to make an enquiry about the buyer.

SAMPLE EXPORTS

The foreign customer may ask for product samples before placing a confirmed order. So, it is essential that the samples are made from good quality raw materials and after getting an order, the subsequent goods are made with the same quality product. While sending a product sample to an importer, it is always advised to send samples by air mail to avoid undue delay.

Sending Export Samples from India

Samples having permanent marking as "sample not for sale" are allowed freely for export without any limit. However, in such cases where indelible marking is not available, the samples may be allowed for a value not exceeding US $ 10,000, per consignment. For export of sample products which are restricted for export as mentioned in the ITC (HS) Code, an application may be made to the office of Director General of Foreign Trade (DGFT).

Export of samples to be sent by post parcel or air freight

Export of samples to be sent by post parcel or air freight is further divided into following 3 categories, and under each category an exporter is required to fulfill certain formalities which are mentioned below :

- **Samples of value up to Rs.10,000**- It is necessary for the exporter to file a simple declaration that the sample does not involve foreign exchange and its value is less than Rs. 10,000.
- **Samples of value less than Rs. 25,000**- It is necessary for the exporter to obtain a value certificate from the authorised dealer in foreign exchange (i.e. your bank). For this purpose, an exporter should submit a commercial invoice certifying thereon that the parcel does not involve foreign exchange and the aggregate value of the samples exported by you does not exceed Rs. 25,000 in the current calendar year.

– **Samples of value more than Rs. 25,000**- It becomes necessary for the exporter to obtain GR/PP waiver from the Reserve Bank of India

Export Samples against Payment

A sample against which an overseas buyer agrees to make payment is exported in the same manner as the normal goods are exported. Sample can also be carried personally by exporter while travelling abroad provided these are otherwise permissible or cleared for export as explained earlier. However, in case of precious jewellery or stone the necessary information should be declared to the custom authorities while leaving the country and obtain necessary endorsement on export certificate issued by the Jewelry Appraiser of the Customs.

Export of Garment Samples

As per the special provision made for the export of garment samples, only those exporters are allowed to send samples that are registered with the Apparel export Promotion Council (AEPC). Similarly, for export of wool it is necessary for the exporter to have registration with the Woolen Export Promotion Council.

Export of Software Samples

All kinds electronic and computer software product samples can only be exported abroad, if the exporter dealing with these products is registered with the Electronics and Computer Software Export Promotion Council (ESC). Similarly samples of other export products can be exported abroad under the membership of various Export Promotion Councils (EPC) of India.

EXPORT PRICING

Export pricing is the most important factor in for promoting export and facing international trade competition. It is important for the exporter to keep the prices down keeping in mind all export benefits and expenses. However, there is no fixed formula for successful export pricing and it differs from exporter to exporter depending upon whether the exporter is a merchant exporter or a manufacturer exporter or exporting through a canalising agency. Export Pricing can be determined by the following factors:

– Range of products offered.
– Prompt deliveries and continuity in supply.
– After-sales service in products like machine tools, consumer durables.
– Product differentiation and brand image.
– Frequency of purchase.
– Presumed relationship between quality and price.
– Specialty value goods and gift items.
– Credit offered.
– Preference or prejudice for products originating from a particular source.
– Aggressive marketing and sales promotion.
– Prompt acceptance and settlement of claims.
– Unique value goods and gift items.

As regards quoting the prices to the overseas buyer, the same are quoted in the following internationally accepted terms which are commonly known as Incoterms.

INCOTERMS

The Incoterms rules are an internationally recognized standard and are used worldwide in international and domestic contracts for the sale of goods. Incoterms are a set of three-letter standard trade terms most commonly used in international contracts for the sale of goods. Incoterms are accepted by governments, legal authorities and practitioners worldwide for the interpretation of the most commonly used terms in international trade. They either reduce or remove altogether uncertainties arising from differing interpretations of such terms in different countries. Incoterms rules provide internationally accepted definitions and rules of interpretation for most common commercial terms. They help traders avoid costly misunderstandings by clarifying the tasks, costs and risks involved in the delivery of goods from sellers to buyers. Incoterms rules are recognized by UNCITRAL as the global standard for the interpretation of the most common terms in foreign trade.

Incoterms were first published in 1936 by the International Chamber of Commerce (ICC). The rules have been developed and maintained by experts and practitioners brought together by ICC and have become the standard in international business rules setting. Incoterms rules are periodically revised to ensure that they are kept up to date with current trade practices. Multiple versions of Incoterms like Incoterms 2000, Incoterms 2010 are available for use by contracting parties. The Incoterms 2010 rules are effective from January 1, 2011. It is recommend using Incoterms 2010 after 2011. However parties can choose earlier version of Incoterms also. But it is important to clearly specify the chosen version of Incoterms.

Scope

The scope of Incoterms is limited to matters relating to the rights and obligations of the parties to the contract of sale with respect to the delivery of goods sold, but excluding "intangibles" like computer software.The Incoterms rules have become an essential part of the daily language of trade. They have been incorporated in contracts for the sale of goods worldwide and provide rules and guidance to importers, exporters, lawyers, transporters, insurers and students of international trade.

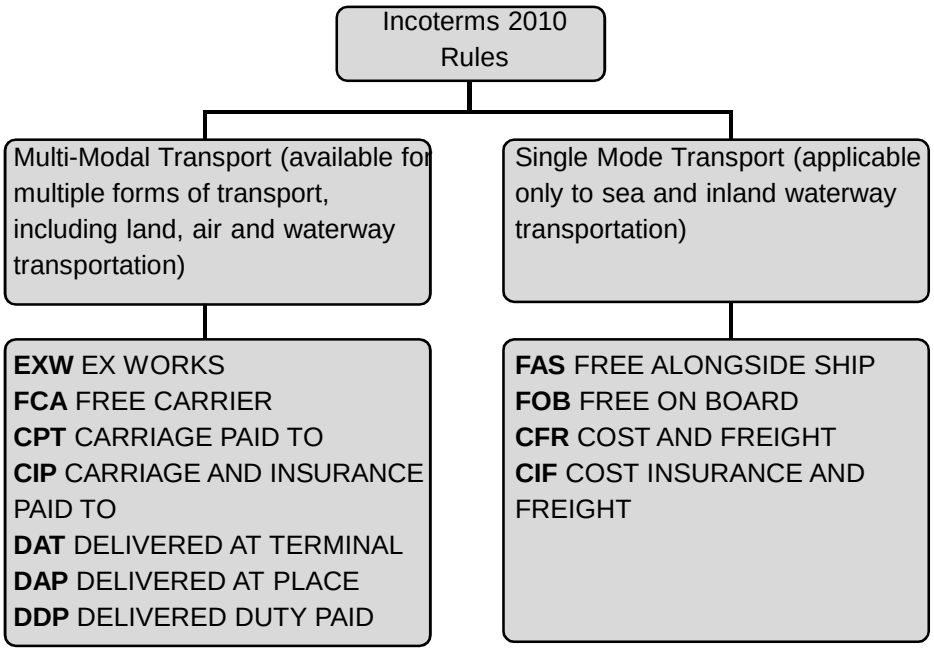
The terms are structured to increase incrementally the obligations (control, risk and cost) on one party while decreasing the obligations of the other, depending on the specific term chosen. Each term clarifies which party is responsible for:

- Inland freight (transportation within the origination country)
- Forwarder selection
- Export clearance
- Carrier selection and scheduling
- International freight
- Import clearance
- On-carriage (transportation within the destination country)

Delivery occurs (and risk of loss transfers) at the point designated by the term selected. Transfer of title is NOT covered by any of the Incoterms 2010 rules and must be separately specified by the parties.

Classification of the Incoterms 2010 rules

The Incoterms 2010 rules are presented in two distinct classes. The terms in each group are listed below in order of increasing responsibility for the seller (and correspondingly decreasing responsibility for the buyer). So, for example, using the term EXW makes the seller responsible only for making the goods available at its own premises; delivery occurs and risk of loss transfers at that point. When the term DDP is used, the seller becomes responsible for everything except on-carriage where the location for delivery is not the buyer’s actual location. DDP is the only Incoterms® rule that makes the seller responsible for import clearance.



Rules for any mode or modes of transport/Multi modal transport

The first class includes the seven Incoterms 2010 rules that can be used irrespective of the mode of transport selected and irrespective of whether one or more than one mode of transport is employed. They can be used even when there is no maritime transport at all. It is important to remember, however, that these rules can be used in cases where a ship is used for part of the carriage.

1. EXW – EX WORKS (… named place of delivery)

The Seller's only responsibility is to make the goods available at the Seller's premises. The Buyer bears full costs and risks of moving the goods from there to destination.

2. FCA – FREE CARRIER (… named place of delivery)

The Seller delivers the goods, cleared for export, to the carrier selected by the Buyer. The Seller loads the goods if the carrier pickup is at the Seller's premises. From that point, the Buyer bears the costs and risks of moving the goods to destination.

3. CPT – CARRIAGE PAID TO (… named place of destination)

The Seller pays for moving the goods to destination. From the time the goods are transferred to the first carrier, the Buyer bears the risks of loss or damage.

4. CIP– CARRIAGE AND INSURANCE PAID TO (… named place of destination)

The Seller pays for moving the goods to destination. From the time the goods are transferred to the first carrier, the Buyer bears the risks of loss or damage. The Seller, however, purchases the cargo insurance.

5. DAT – DELIVERED AT TERMINAL (… named terminal at port or place of destination)

The Seller delivers when the goods, once unloaded from the arriving means of transport, are placed at the Buyer's disposal at a named terminal at the named port or place of destination. "Terminal" includes any place, whether covered or not, such as a quay, warehouse, container yard or road, rail or air cargo terminal. The Seller bears all risks involved in bringing the goods to and unloading them at the terminal at the named port or place of destination.

6. DAP – DELIVERED AT PLACE (… named place of destination)

The Seller delivers when the goods are placed at the Buyer's disposal on the arriving means of transport ready for unloading at the names place of destination. The Seller bears all risks involved in bringing the goods to the named place.

7. DDP – DELIVERED DUTY PAID (… named place)

The Seller delivers the goods -cleared for import – to the Buyer at destination. The Seller bears all costs and risks of moving the goods to destination, including the payment of Customs duties and taxes.

Rules for Sea and Inland Waterway Transport

In the second class of Incoterms 2010 rules, the point of delivery and the place to which the goods are carried to the buyer are both ports, hence the label "sea and inland waterway" rules. FAS, FOB, CFR and CIF belong to this class. The last three Incoterms rules consider the goods being delivered when they are "on board" on the vessel. The ship's rail as the point of delivery has been omitted in these rules which more closely reflects modern commercial reality and avoids the rather dated image of the risk of transfer.

1. FAS – FREE ALONGSIDE SHIP (… named port of shipment)

The Seller delivers the goods to the origin port. From that point, the Buyer bears all costs and risks of loss or damage.

2. FOB– FREE ON BOARD (… named port of shipment)

The Seller delivers the goods on board the ship and clears the goods for export. From that point, the Buyer bears all costs and risks of loss or damage.

3. CFR– COST AND FREIGHT (… named port of destination)

The Seller clears the goods for export and pays the costs of moving the goods to destination. The Buyer bears all risks of loss or damage.

4. CIF – COST INSURANCE AND FREIGHT (… named port of destination)

The Seller clears the goods for export and pays the costs of moving the goods to the port of destination. The Buyer bears all risks of loss or damage. The Seller, however, purchases the cargo insurance.

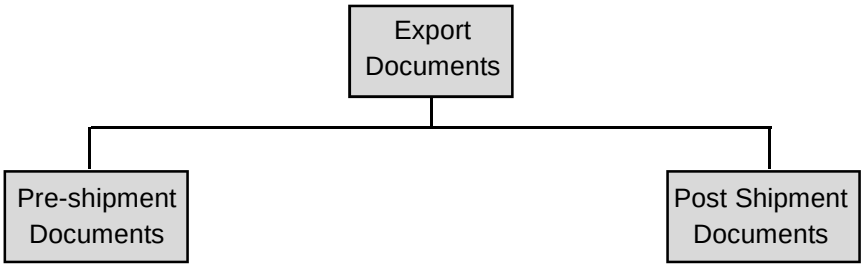
Rules for domestic and international trade

Incoterms rules have traditionally been used in international sale contracts where goods pass across national borders. In various areas of the world, however, trade blocs, like the European Union, have made border formalities between different countries less significant. Consequently, the subtitle of the Incoterm 2010 rules formally recognizes that they are available for application to both international and domestic sale contracts. Two developments have persuaded the ICC that a movement in this direction is timely. Firstly, traders commonly use Incoterms rules for purely domestic sale contracts. The second reason is the greater willingness in the United States to use Incoterms rules in domestic trade rather than the former Uniform Commercial Code shipment and delivery terms. As a result, the Incoterms 2010 rules clearly state in a number of places that the obligation to comply with export/import formalities exists only where applicable.

EXPORT DOCUMENTS

Risks are inherent in both domestic trade and international trade, but the degree of risk is higher in international trade. Hence, proper documentation mitigates the risk in international trade. Documentation must be precise. Slight discrepancies or omissions may prevent merchandise from being exported or result in exporting firms not getting paid, or even result in the seizure of the exporter's goods by local or foreign government customs.

Collection documents are subject to precise time limits and may not be honoured by a bank, if out of date. Much of the documentation is routine for the freight forwarders or customs brokers acting on the firm's behalf, but the exporter is ultimately responsible for the accuracy of the documentation. **It is said that "International Trade is a sale of documents"**. It is very important to clearly understand the documents involved in the transaction to avoid the risk factors and adhere to the legal obligations. The entire documentation in export trade can be basically divided into two categories:



Pre-shipment Documents

Pre-shipment documents are those that an exporter has to generate, authenticate and submit to the concerned authorities and departments to get the necessary clearances, prior to the actual shipment of the cargo, so that the cargo can be shipped out with valid documents. The pre-shipment documents are generally prepared when the product is ready for export and prior to shipment. The standard pre-shipment documents include:

- Customs Invoice
- Packing List
- GP Form (original and duplicate)
- AR4 Form (original and duplicate)
- Copy Of Export order
- Letter Of Credit
- Shipping Bill (entire set)
- Export Licence(for notified items)
- Certificate Of Origin
- Certificate Of Inspection
- Any Other Documents (as required in L/C or by Customs)

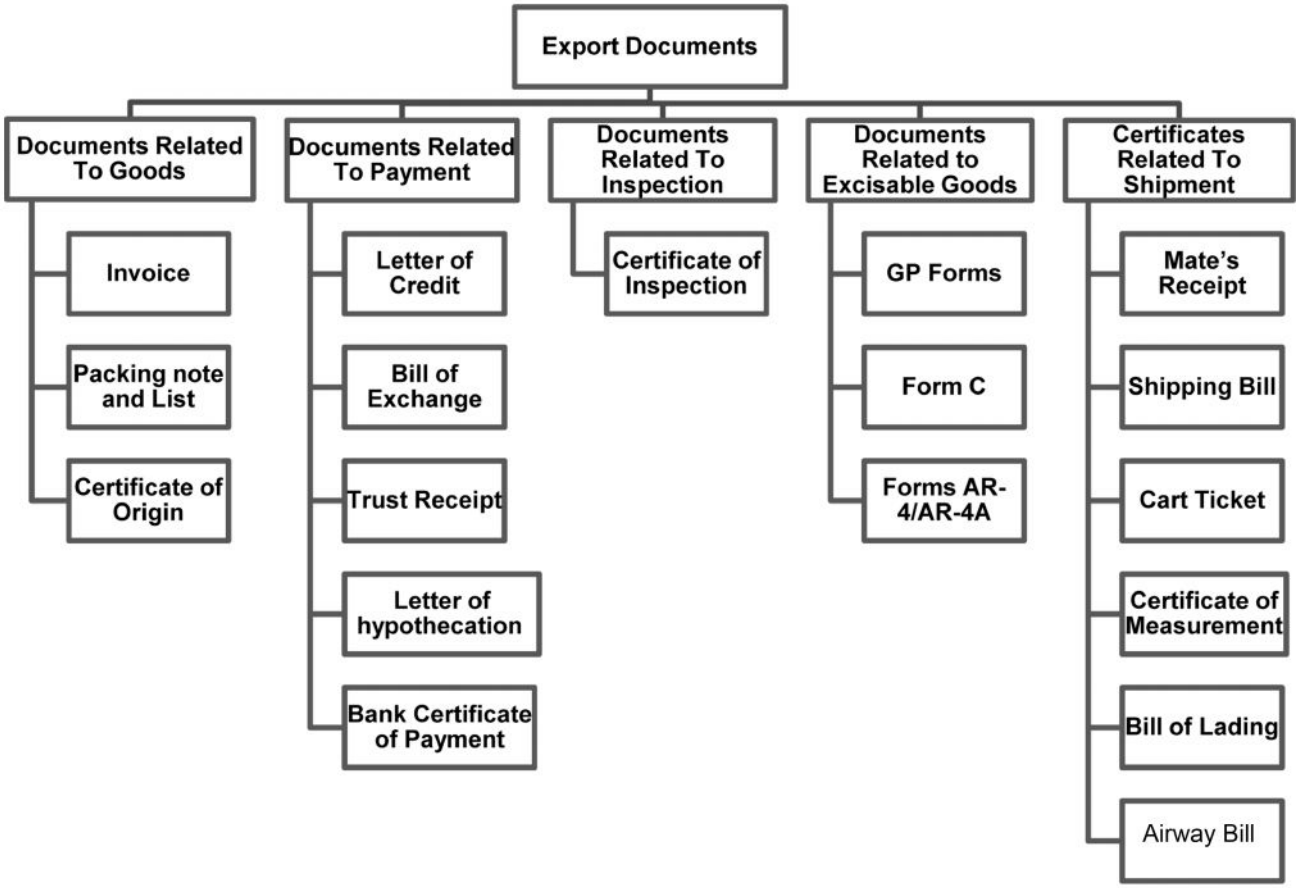
Post Shipment Documents

The post-shipment documents comprise the certified copies of some of the main pre-shipment documents and certain additional documents to be generated and compiled by the exporter so that the proof of shipments can be properly presented to the negotiating bank for collecting the payments through L/C or for presentation to the foreign buyer for collection of payment through the nominated bank. The standard pre-shipment documents include

- Custom attested invoice
- Custom attested packing list
- Copy of Export Order / Copy Of LC

- Commercial Invoice
- Consular Invoice (If Specified)
- Bill of Lading / Air Way Bill
- Certificate of Origin
- Certificate of Inspection (If Specified)
- Bill of Exchange (Draft)
- GP Form (Duplicate)
- Any other document specified in Export Order / LC Export from India required special documents depending upon the type of product and destination to be exported. These documents are as follows:

The export documents can also be divided on the basis given in the diagram below:



DOCUMENTS RELATED TO GOODS

(i) Invoice: An invoice is the seller's bill for merchandise and contains particulars of goods, such as the price per unit at a particular location, quantity, total value, packing specifications, terms of sale, identification marks of the package, bill of landing number, name and address of importer, destination, name of the ship, etc.

(ii) Packing note and List: The difference between a packing note and a packing list is that the packing note; refers to the particular of the contents of an individual pack, while the packing list is a consolidated statement of the contents of a number of cases or packs.

A packing note should, include the packing note number, the date of packing, the name and address of the exporter, the name and address of the importer, the order number, date, shipment per S/S, bill of lading number and date, marking numbers, case number to which the note relates, and the contents of the goods in terms of quantity and weight. Apart from the details in the packing note, a packing list should also include item wise details.

No particular form has been prescribed for the packing note or packing list. Normally, ten copies of the packing note/list should be prepared. The first is to be sent with the shipping documents, two copies in advance to the buyer, one to the shipping agent and the remaining retained by the exporter.

(iii) Certificate of Origin: A certificate of origin, as the name indicates, is a certificate which specifies the country of the production of the goods. This certificate has also to be produced before clearance of goods and assessment of duty, for the customs law of the country offers a preferential tariff to India and the former is to ensure that only goods of Indian origin benefit from such concession. A certificate of origin may be required when goods of a particular type from certain countries are banned.

A certificate of origin form may be obtained from Chambers of Commerce, Export Promotion Councils, and various trade associations which have been authorized by the Government.

DOCUMENTS RELATED TO PAYMENT

(i) Letter of Credit: A letter of credit is a document containing the guarantee of a bank to honour drafts drawn on it by an exporter, under certain conditions and up to certain amounts, provided that the beneficiary fulfils the stipulated conditions. For details of the letter of credit and the use of the letter of credit in financing foreign trade, see Annexure to the Chapter on Export Financing.

(ii) Bill of Exchange: The Negotiable Instruments Act, 1881, defines the bill of exchange as “an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument.

(iii) Trust Receipt : If the importer is unable to take possession of the documents by making the payment on the D/P bill following the arrival of the goods, the merchandise may be made available to the importer by his bank under an arrangement whereby the importer signs a trust receipt. Under this arrangement, the importer is allowed to sell the imported good by acting as an agent of the bank; but the retains ownership of the merchandise until the importer has made full settlement; all sums received from the sale of goods must be credited to the bank until such settlement is made.

(iv) Letter of hypothecation: A letter of hypothecation is a document signed by the customer covenying to a banker the full ownership of goods at the port of destination in respect of which he has made advances either by loan or by acceptance or negotiation of bills of exchange. This is a sort of blanket document which any banker, who accepts bills, advances money or negotiates bills and shipping documents, demands from a customer to give him recourse on the bills and control of the documents. The letter of hypothecation pledges the documents of title with the banker as security for an advance and gives the bank power to sell the goods. If necessary, to insure them and to warehouse them at the customer’s expense.

(v) Bank Certificate of Payment: It is a certificate issued by the negotiating bank of the exporter, certifying that the bill covering particular consignments, has been negotiated and that the proceeds received in accordance with exchange control regulations in the approved manner.

DOCUMENTS RELATED TO INSPECTION

(i) Certificate of Inspection: It is certificate issued by the Export Inspection Agency, certifying that the consignment has been inspected as required under the Export (Quality Control and Inspection) Act, 1963, and satisfies the conditions relating to quality control and inspection as applicable to it, and is certified export worthy.

DOCUMENTS RELATED TO EXCISABLE GOODS

(i) GP Forms : A GP form is a gate pass for the removal of excisable goods from a factory or warehouse. Form GP1 is used for the removal of excisable goods on payment of duty and form GP2 is used for the removal of excisable goods without payment of duty.

(ii) Form C : Form C is to be used for applying for rebate of duty on the excisable goods (other than vegetable, non-essential oils and tea) exported by sea. It is to be submitted in triplicate to the Collector of Central Excises.

(iii) Forms AR-4/AR-4A : These forms are meant for applying for the removal of excisable goods for export by sea/post. Form Ar-4 is used for applying for excise inspection at the factory and form AR-4A is used when goods are to be exported under a claim for rebate of excise duty or under bond.

CERTIFICATES RELATED TO SHIPMENT

(i) Mate's Receipt: A mate's receipt is a receipt issued by the Commanding Office of the ship when the cargo is loaded on the ship, and contains information about the name of the vessel, berth, date of shipment, description of packages, marks and numbers, condition of the cargo at the time of receipt on board the ship, etc.

The mate receipt is first handed over to the Port Trust authorities so that all the port dues may be paid by the exporter. After paying all the port dues, the merchant or the agent may collect the mate's receipt from the Port Trust authorities. The bill of lading is prepared by the shipping agent after the mate's has been obtained.

(ii) Shipping Bill: The shipping bill is the main document on the basis of which the Customs' permission for export is given. The shipping bill contains particulars of the goods exported, the name of the vessel, master or agents, flag, the port at which goods are to be discharged, the country of final destination, the exporter's name and address, etc., It also contains details of the packages and the goods, such as number and description, marks and numbers, quantity details about each case, f.o.b., prices, real value as defined in the Sea Customs Act, whether Indian or foreign merchandise to be re-exported, total number of packages, their total weight and value, etc. The following three forms of the shipping bill are available with the Customs authorities :

- Dutiable shipping bill for goods for which there is export duty.
- Free shipping bill for goods for which there is no export duty.
- Drawback shipping bill which is required for claiming the Customs drawback against goods exported.

(iii) Cart Ticket: A cart ticket, also known as a cart chit, vehicle and gate pass, is prepared by the exporter and includes details of the export cargo in terms of the shipper's name, the number of packages, the shipping bill number, the port of destination and the number of the vehicle carrying the cargo. The driver of the vehicle carrying cargo should possess the ticket, and when the vehicle is brought at the port gate, it should be presented to the gate warden/inspector/keeper along with other shipping and port documents. The gate keeper/warden/ inspector, after satisfying himself that the vehicle is carrying the cargo as mentioned in the document, allows it to pass the gate.

(iv) Certificate of Measurement: Freight is charged either on the basis of weight or measurement. When it is charged on the basis of weight, the weight declared by the shipper may be accepted. However, a certificate of measurement from the Indian Chamber of Commerce or other approved organization may be obtained by the shipper and given to the shipping company for the calculation of the necessary freight. The certificate contains the name of the vessel, port and destination, the description of goods, the quantity, length, breadth, depth, etc., of the packages.

(v) Bill of Lading: The bill of lading is a document wherein the shipping company gives its official receipts of the goods shipped in its vessel and at the same time contracts to carry them to the port of destination. It is also a document of title to the goods and, as such, is freely transferable by endorsement and delivery. A bill of lading serves three main purposes:

– As a document of title to the goods;

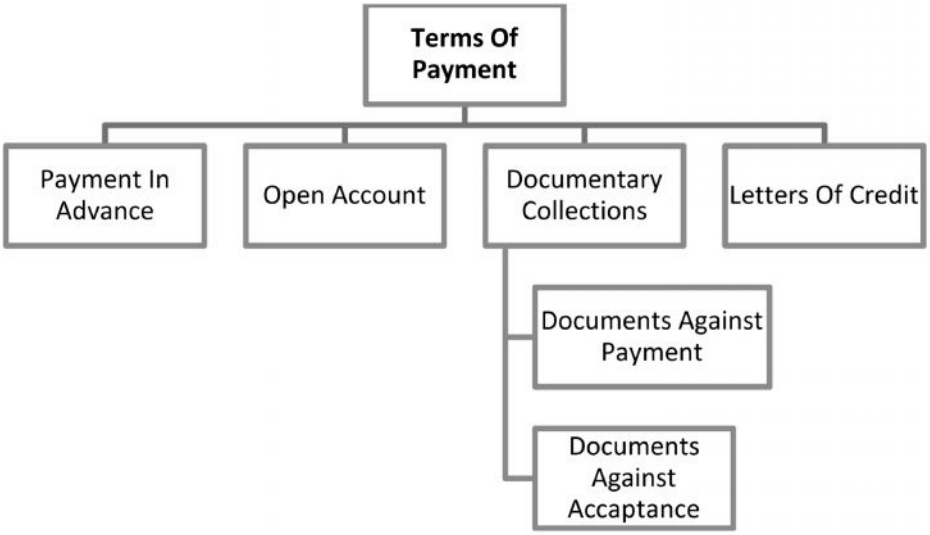
– As a receipt from the shipping company; and

– As a contact for the transportation of goods.

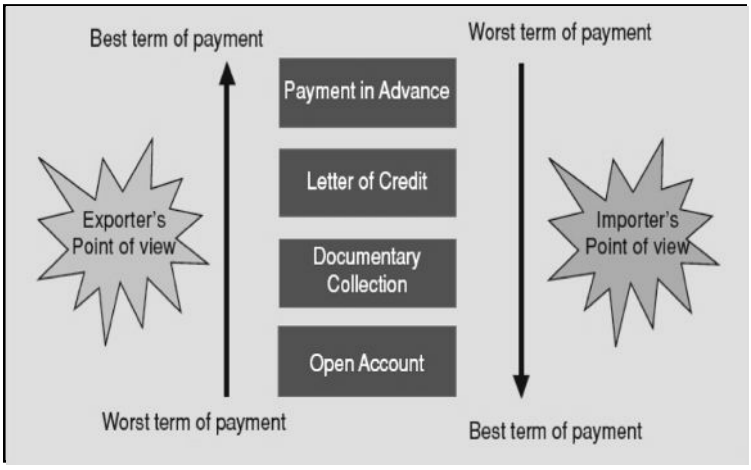
(vi) Airway Bill: An airway bill, also called, an air consignment note, is a receipt issued by an airline for the carriage of goods. As each shipping company has its own bill of lading, each airline has its own airway bill.

TERMS OF PAYMENT OR METHODS OF PAYMENT

When negotiating a contract, supplier and buyer will have to agree on the terms of payment. Generally, there are four types of payment terms:



Each of the four payment methods described above carries associated risks and offers a different level of protection to importers and exporters. For example, a payment method that is considered risk-free for the exporter (e.g., advance payment) is considered very risky for the importer. The crucial question is who will bear the credit risk? When an exporter sells on open account or consignment basis, the exporter bears the entire credit risk. On the other hand, in cases when the importer makes advance payment at the time of placing the order, he bears the credit risk. Most often, given the complexities in cross-border transactions and the absence of detailed knowledge regarding the financial status of the two parties, credit risk will be shifted to an intermediary who specializes in evaluating and undertaking such risks. This may be a government institution such as an EXIM bank in India or commercial banks, factors or others.



The determination of payment terms would also depend upon the nature of the relationship between the exporter and importer.

- If the foreign importer is unaffiliated unknown party with whom no business has been done before, it is best for exporter to choose advance payment.
- If the foreign importer is unaffiliated but known party with whom business has been done before, the exporter can choose between letter of credit or documentary collections depending upon the terms and relationship between the parties.
- If the foreign importer is a subsidiary business unit of the exporting firm, open account method can also be suitable from exporter's point of view.

Thus the selection of term of payment should be done keeping in mind all the relevant factors to avoid risk of loss in international trade.

PAYMENT IN ADVANCE

Payment in advance, or advance payment, refers to a situation in which the seller requests payment from the buyer before he will ship the goods. The seller only ships out the goods to the buyer after receiving the payment. The settlement method used is likely to be SWIFT payment, telegraphic transfer or bank draft.

Some best practices for advance payment

Seller:

- Give the buyer clear payment instructions, including mode of payment (for example, by SWIFT).
- Avoid accepting bank drafts (cheques) or company cheques.
- If you are asked to issue an advance payment guarantee, instruct your bank to make the guarantee "inoperative" until you receive the payment.

Buyer:

- Avoid this arrangement. Try offering a letter of credit instead.
- Insist on an advance payment guarantee. This will allow you to recover the payment if the seller fails to fulfil his part of the contract.

OPEN ACCOUNT

In an open account transaction, the seller ships the goods together with the necessary documents to the buyer before the payment is made and without any form of guarantee. When the goods have been dispatched, the seller also sends the buyer an invoice asking for payment within the agreed credit terms, for example, 60 days from the invoice date.

Some best practices for open accounts

Seller:

- Do not agree to an open account when the buyer is new to you or you are unable to determine the risk or the reliability of the buyer.
- Keep in mind that your goods are delivered before payment; therefore, make sure that you supply your goods or services in accordance with the contract terms, thus avoiding disputes and non-payment.
- Insist on an electronic transfer (cleared funds) instead of a bank draft or cheque (uncleared funds).

Buyer:

- Make sure that the goods or services are satisfactory before you effect payment.
- Make sure that payment is made in accordance with the agreed credit terms to avoid damaging your trading relationship with the supplier.
- Make sure to pay according to the settlement instructions.

DOCUMENTARY COLLECTIONS

Documentary collection offers some protection to the seller. It is more secure than shipping on an open account basis but less secure than using a letter of credit or an advance payment. A documentary collection (D/C) is a transaction whereby the exporter entrusts the collection of payment to the remitting bank (exporter's bank), which sends documents to a collecting bank (importer's bank), along with instructions for payment. Funds are received from the importer and remitted to the exporter through the banks involved in the collection in exchange for those documents. D/Cs involve the use of a draft that requires the importer to pay the face amount either on sight (document against payment—D/P) or on a specified date in the future (document against acceptance—D/A). The draft lists instructions that specify the documents required for the transfer of title to the goods. Although banks do act as facilitators for their clients under collections, documentary collections offer no verification process and limited recourse in the event of non-payment.

- D/Cs are less complicated and less expensive than LCs.
- Under a D/C transaction, the importer is not obligated to pay for goods prior to shipment.
- The exporter retains title to the goods until the importer either pays the face amount on sight or accepts the draft to incur a legal obligation to pay at a specified later date.
- Banks that play essential roles in transactions utilizing D/Cs are the remitting bank (exporter's bank) and the collecting bank (importer's bank).
- While the banks control the flow of documents, they do not verify the documents nor take any risks, but can influence the mutually satisfactory settlement of a D/C transaction.

When to Use Documentary Collections

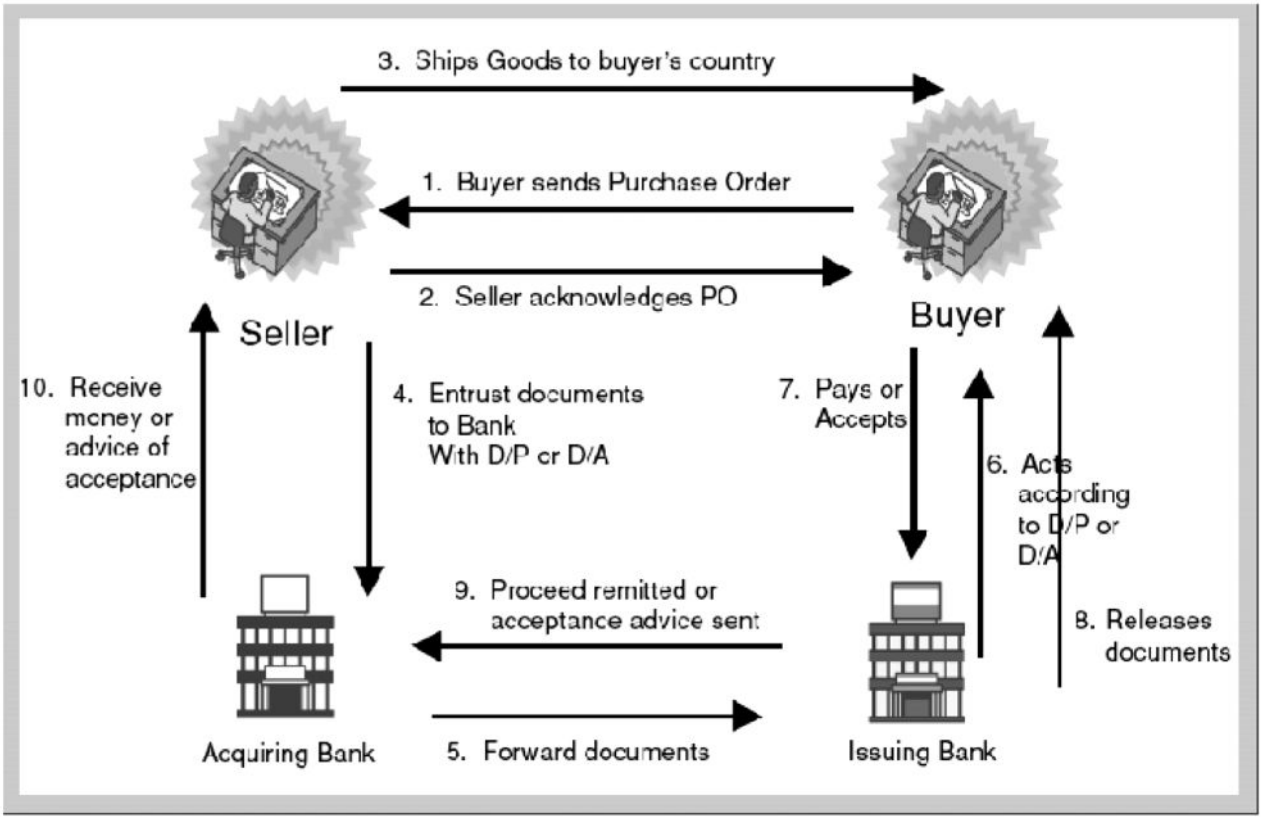
Under D/C transactions, the exporter has little recourse against the importer in case of nonpayment. Thus, the D/C mechanism should only be used under the following conditions:

- The exporter and importer have a well-established relationship.
- The exporter is confident that the importing country is stable politically and economically.
- An open account sale is considered too risky, but an LC is also too expensive for the importer.

Typical steps in D/C Transaction Flow are given below:

1. The exporter ships the goods to the importer and receives in exchange the documents.
2. The exporter presents the documents with instructions for obtaining payment to its bank.
3. The exporter's remitting bank sends the documents to the importer's collecting bank.
4. The collecting bank releases the documents to the importer upon receipt of payment.
5. Or the collecting bank releases the documents on acceptance of draft from the importer.
6. The importer then presents the documents to the carrier in exchange for the goods.
7. Having received payment, the collecting bank forwards proceeds to the remitting bank.

8. Once payment is received, the remitting bank credits the exporter's account.



Documents Against Payment (D/P)

Under a D/P collection, the exporter ships the goods, and then gives the documents to his bank, which will forward them to the importer's collecting bank, along with instructions on how to collect the money from the importer. In this arrangement, the collecting bank releases the documents to the importer only on payment for the goods. Upon receipt of payment, the collecting bank transmits the funds to the remitting bank for payment to the exporter.

- Time of Payment: After shipment, but before documents are released
- Transfer of Goods: After payment is made on sight
- Exporter Risk: If draft is unpaid, goods may need to be disposed

Documents Against Acceptance (D/A)

Under a D/A collection, the exporter extends credit to the importer by using a time draft. In this case, the documents are released to the importer to receive the goods upon acceptance of the time draft. By accepting the draft, the importer becomes legally obligated to pay at a future date. At maturity, the collecting bank contacts the importer for payment. Upon receipt of payment, the collecting bank transmits the funds to the remitting bank for payment to the exporter. In the case of D/A, a bill of exchange accompanies the collection order. A bill of exchange is a written order addressed by the seller to the buyer, asking the buyer to pay a certain amount of money on a specified date. By accepting the bill of exchange, the buyer agrees to pay on that date. The documents are released to the buyer when he or she accepts the bill, in which case the buyer's bank holds the bill until it matures (ends) and the buyer pays the seller.

- Time of Payment: On maturity of draft at a specified future date
- Transfer of Goods: Before payment, but upon acceptance of draft

– Exporter Risk: Has no control of goods and may not get paid at due date

Some best practices for collections

Seller:

– Make sure that you are satisfied with the buyer and country risks before agreeing to this method.

– Make sure that you supply your goods and services in accordance with the contract terms in order to avoid disputes.

– Make sure that your collection instructions are clear and match the terms of the contract exactly.

Buyer:

– When you are asked to pay or accept the bill of exchange, make sure that the terms are exactly as you agreed in the contract.

– If possible, make sure that the goods or services are satisfactory before you instruct your bank to pay or before you accept the bill of exchange.

– Make sure that you have received the correct documents needed to obtain the goods. Once you are satisfied that everything is in order, respond promptly when asked to pay or accept the bill of exchange

LETTER OF CREDIT

A Letter of Credit, simply defined, is a written instrument issued by a bank at the request of its customer, the Importer (Buyer), whereby the bank promises to pay the Exporter (Beneficiary) for goods or services, provided that the Exporter presents all documents called for, exactly as stipulated in the Letter of Credit, and meet all other terms and conditions set out in the Letter of Credit. A Letter of Credit is also commonly referred to as a Documentary Credit.

The International Chamber of Commerce (ICC) in the Uniform Custom and Practice for Documentary Credit (UCPDC) defines documentary credit as:

> "An arrangement, however named or described, whereby a bank (the issuing bank) acting at the request and in accordance with the instructions of a customer (the applicant to the credit) to make payment to or to the order third party (the beneficiary) or is to pay, accept or negotiate bills of exchange (drafts) drawn by the beneficiary, or authorise such payments to be made or such drafts to be paid, accepted or negotiated, by another bank, against stipulated documents and compliance with stipulated terms and conditions."

Letters of credit (LCs) are among the most secure instruments available to international traders. An LC is a commitment by a bank on behalf of the buyer that payment will be made to the beneficiary (exporter) provided that the terms and conditions have been met, as verified through the presentation of all required documents. The buyer pays its bank to render this service. An LC is useful when reliable credit information about a foreign buyer is difficult to obtain, but you are satisfied with the creditworthiness of your buyer's foreign bank. This method also protects the buyer, since no payment obligation arises until the documents proving that the goods have been shipped or delivered as promised are presented. However, since LCs have many opportunities for discrepancies, they should be prepared by well-trained documenters or the function may need to be outsourced.

– An LC, also referred to as a documentary credit, is a contractual agreement whereby a bank in the buyer's country, known as the issuing bank, acting on behalf of its customer (the buyer or importer), authorizes a bank in the seller's country, known as the advising bank, to make payment to the beneficiary (the seller or exporter) against the receipt of stipulated documents.

– The LC is a separate contract from the sales contract on which it is based and, therefore, the bank is not concerned whether each party fulfils the terms of the sales contract.

– The bank's obligation to pay is solely conditional upon the seller's compliance with the terms and conditions of the LC. In LC transactions, banks deal in documents only, not goods.

Parties to Letters of Credit

– ***Applicant (Opener)*****:** The Applicant which is also referred to as a buyer or customer or importer of the goods, who has to make payment to beneficiary. LC is initiated and issued at his request and on the basis of his instructions.

– ***Issuing Bank (Opening Bank)*****:** The issuing bank is the one which create a letter of credit and takes the responsibility to make the payments on receipt of the documents from the beneficiary or through their banker. The payments has to be made to the beneficiary within seven working days from the date of receipt of documents at their end, provided the documents are in accordance with the terms and conditions of the letter of credit. If the documents are discrepant one, the rejection thereof to be communicated within seven working days from the date of of receipt of documents at their end.

– ***Beneficiary*****:** The Beneficiary is normally the seller exporter of the goods, who has to receive payment from the applicant. A credit is issued in his favour to enable him or his agent to obtain payment on surrender of stipulated documents and complying with the term and conditions of the L/c. If L/c is a transferable one and he transfers the credit to another party, then he is referred to as the first or original beneficiary.

The three parties mentioned above are regarded as the fundamental parties. However, following parties are also concerned with a Letter of Credit Transaction.

– ***Advising Bank*****:** The Advising Bank provides advice to the beneficiary and takes the responsibility for sending the documents to the issuing bank and is normally located in the country of the beneficiary.

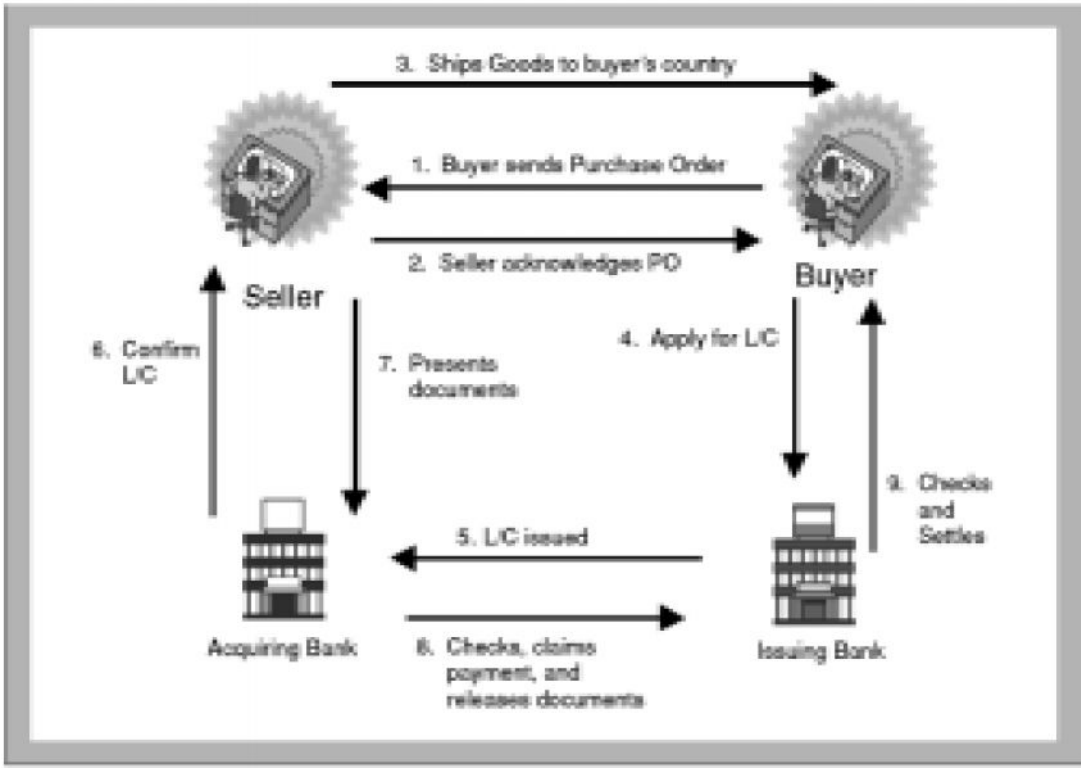
– ***Confirming Bank*****:** The Confirming bank adds its guarantee to the credit opened by another bank, thereby undertaking the responsibility of payment/negotiation acceptance under the credit, in additional to that of the issuing bank. Confirming bank play an important role where the exporter is not satisfied with the undertaking of only the issuing bank. It is located in exporter's country. It issuing bank fails, the confirming bank has to honours its commitment.

– ***The Negotiating Bank*****:** The Negotiating Bank is the bank who negotiates the documents submitted to them by the beneficiary under the credit either advised through them or restricted to them for negotiation. On negotiation of the documents they will claim the reimbursement under the credit and makes the payment to the beneficiary provided the documents submitted are in accordance with the terms and conditions of the letters of credit.

– ***The Reimbursing Bank/Paying Bank*** **:** Reimbursing Bank is the bank authorized to honor the reimbursement claim in settlement of negotiation/acceptance/payment lodged with it by the negotiating bank. It is normally the bank with which issuing bank has an account from which payment has to be made.

– ***Second Beneficiary*****:** Second Beneficiary is the person who represent the first or original Beneficiary of credit in his absence. In this case, the credits belonging to the original beneficiary is transferable. The rights of the transferee are subject to terms of transfer.

The following is a step-by-step description of a typical Letter of Credit transaction:



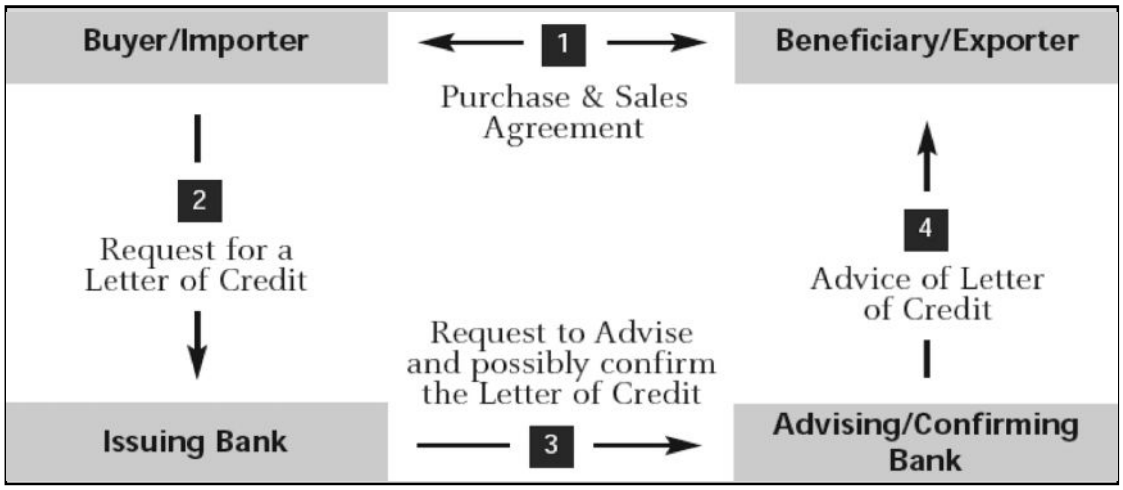
1. An Importer (Buyer) and Exporter (Seller) agree on a purchase and sale of goods where payment is made by Letter of Credit.

2. The Importer completes an application requesting its bank (Issuing Bank) to issue a Letter of Credit in favour of the Exporter. Note that the Importer must have a line of credit with the Issuing Bank in order to request that a Letter of Credit be issued.

3. The Issuing Bank issues the Letter of Credit and sends it to the Advising Bank by telecommunication or registered mail in accordance with the Importer's instructions. A request may be included for the Advising Bank to add its confirmation. The Advising Bank is typically located in the country where the Exporter carries on business and may be the Exporter's bank but it does not have be.

4. The Advising Bank will verify the Letter of Credit for authenticity and send a copy to the Exporter.

Issuance of a letter of a credit



5. The Exporter examines the Letter of Credit to ensure:

- it corresponds to the terms and conditions in the purchase and sale agreement;
- documents stipulated in the Letter of Credit can be produced; and
- the terms and conditions of the Letter of Credit may be fulfilled.

6. If the Exporter is unable to comply with any term or condition of the Letter of Credit or if the Letter of Credit differs from the purchase and sale agreement, the Exporter should immediately notify the Importer and request an amendment to the Letter of Credit.

7. When all parties agree to the amendments, they are incorporated into the terms of the Letter of Credit and advised to the Exporter through the Advising Bank. It is recommended that the Exporter does not make any shipments against the Letter of Credit until the required amendments have been received.

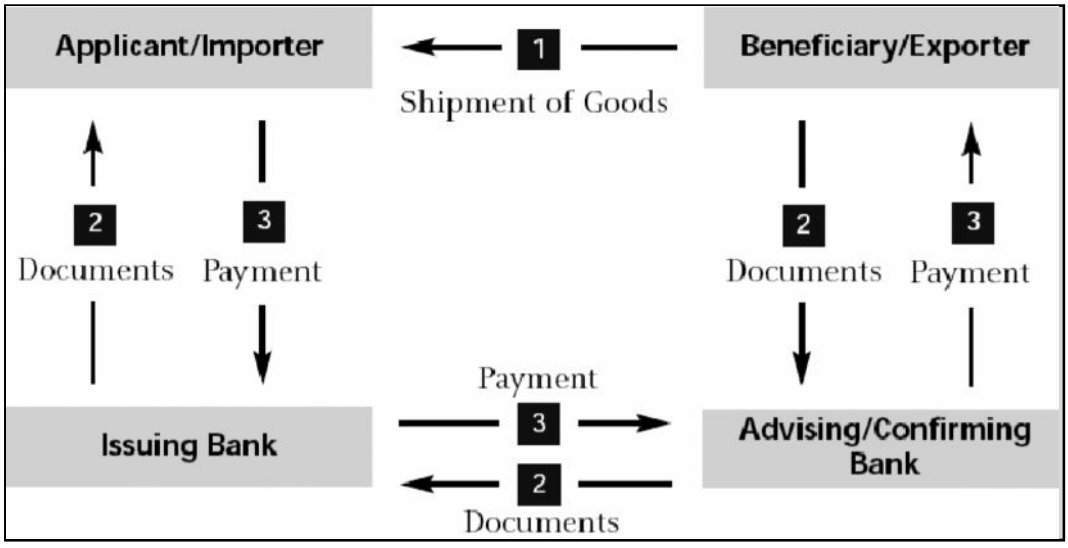
8. The Exporter arranges for shipment of the goods, prepares and/or obtains the documents specified in the Letter of Credit and makes demand under the Letter of Credit by presenting the documents within the stated period and before the expiry date to the "available with" Bank. This may be the Advising/Confirming Bank. That bank checks the documents against the Letter of Credit and forwards them to the Issuing Bank. The drawing is negotiated, paid or accepted as the case may be.

9. The Issuing Bank examines the documents to ensure they comply with the Letter of Credit terms and conditions. The Issuing Bank obtains payment from the Importer for payment already made to the "available with" or the Confirming Bank.

10. Documents are delivered to the Importer to allow them to take possession of the goods from the transport company. The trade cycle is complete as the Importer has received its goods and the Exporter has obtained payment.

Note: In the diagram below, the Advising Bank is also acting as the Confirming Bank.

Payment Under a Letter of Credit



A key principle underlying Letters of Credit is that banks deal only in documents and not in goods. The decision to pay under a Letter of Credit is entirely on whether the documents presented to the bank appear on their face to be in accordance with the terms and conditions of the Letter of Credit. It would be prohibitive for the banks to physically check all merchandise shipped under Letters of Credit to ensure merchandise has been shipped exactly as per each Letter of Credit. Accordingly, the integrity of both the Exporter and Importer are very important in a Letter of Credit transaction. The appropriate due diligence should be exercised by both parties.

Advantages to the Importer

- Importer is assured that the Exporter will be paid only if all terms and conditions of the Letter of Credit have been met.
- Importer is able to negotiate more favourable trade terms with the Exporter when payment by Letter of Credit is offered.

Disadvantages to the Importer

- A Letter of Credit does not offer protection to the Importer against the Exporter shipping inferior quality goods and/or a lesser quantity of goods. Consequently, it is important that the Importer performs the appropriate due diligence to assess the reputation of the Exporter. If the Exporter acts fraudulently, the only recourse available to the Importer is through legal proceedings. Note: Added protection to the Importer may be provided by requesting additional documentation in the Letter of Credit, e.g. a Certificate of Inspection
- It is necessary for the Importer to have a line of credit with a bank before the bank is able to issue a Letter of Credit. The amount outstanding under each Letter of Credit issued is applied against this line of credit from the date of issuance until final payment.

Advantages to the Exporter

- The risk of payment relies upon the creditworthiness of the Issuing Bank and the political risk of the Issuing Bank's domicile, and not the creditworthiness of the Importer.
- Exporter agrees in advance to all requirements for payment under the Letter of Credit. If the Letter of Credit is not issued as agreed, the Exporter is not obligated to ship against it.
- Exporter can further reduce foreign political and bank credit risk by requesting confirmation of the Letter of Credit by a Canadian bank.

Disadvantages to the Exporter

- Documents must be prepared and presented in strict compliance with the requirements stipulated in the Letter of Credit.
- Some Importers may not be able to open Letters of Credit due to the lack of credit facilities with their bank which consequently inhibits export growth.

Some best practices for letters of credit

Seller:

- Make sure that a local bank has authenticated the letter of credit. If you receive a letter of credit directly from a foreign bank, forward it to your bank to have its details verified and have it authorized.
- Examine the letter of credit carefully and make sure that it keeps to the terms of the sales contract.
- Make sure that you can present all the documents named.
- Be extremely careful in preparing your documents. Remember that the guarantee is conditional and the bank will effect payment solely on the basis of the documents. If your documents do not keep to the terms of the letter of credit, you lose your guarantee of payment.
- If the political or economic situation in the buyer's country worries you, you should not ship the goods. Asking a reputable bank to confirm the letter of credit may reduce the economic and political risk.

Buyer:

- Check with your bank in good time and make sure that you have enough credit with your bank.
- Be careful in completing your application and make sure that your guarantee is issued according to

the contract terms. The shipment will not take place until the seller is satisfied, so aim to have the guarantee issued in good time and avoid the time and cost of amendments.

- Use the opportunity to negotiate extended credit terms, if possible.
- Make sure that you call for all the necessary documents so that the goods pass to you smoothly.
- Insist on terms that you think are important to protect your interest, such as latest shipment dates or other such terms.

Types of Letter of Credit

1. Revocable Letter of Credit L/c: A revocable letter of credit may be revoked or modified without the consent of the exporter by the issuing bank. It is rarely used in international trade as it is not beneficial for the exporters. There is no provision for confirming revocable credits as per terms of UCPDC, Hence they cannot be confirmed. It should be indicated in LC that the credit is revocable. If there is no such indication the credit will be deemed as irrevocable.

2. Irrevocable Letter of Credit L/c: An irrevocable L/C cannot be revoked or changed without the consent of the issuing bank, the confirming bank, and the beneficiary/exporter. Form an exporters point of view it is believed to be more beneficial. An irrevocable letter of credit from the issuing bank insures the beneficiary that if the required documents are presented and the terms and conditions are complied with, payment will be made.

3. Confirmed Letter of Credit L/c: Confirmed Letter of Credit is a special type of L/c in which another bank apart from the issuing bank has added its guarantee. Although, the cost of confirming by two banks makes it costlier, this type of L/c is more beneficial for the beneficiary as it doubles the guarantee.

4. Sight L/Credit and Usance L/c: Sight credit states that the payments would be made by the issuing bank at sight, on demand or on presentation. The payment is made when documents are presented. In case of usance credit, draft are drawn on the issuing bank or the correspondent bank at specified usance period. The credit will indicate whether the usance draft are to be drawn on the issuing bank or in the case of confirmed credit on the confirming bank. The payment is made at a future fixed time from presentation of documents (eg. 60 days after sight).

5. Back to Back Letter of Credit L/c: Back to Back Letter of Credit is also termed as Countervailing Credit. A credit is known as backtoback credit when a L/c is opened with security of another L/c. A backtoback credit which can also be referred as credit and countercredit is actually a method of financing both sides of a transaction in which a middleman buys goods from one customer and sells them to another. The parties to a BacktoBack Letter of Credit are:

- The buyer and his bank as the issuer of the original Letter of Credit.
- The seller/manufacturer and his bank,
- The manufacturer's subcontractor and his bank.

It is essentially a secondary credit opened by a bank on behalf of the beneficiary of an original credit, in favour of domestic supplier. The original credit backs another credit & faciliates the purchase of another goods from a local supplier by the beneficiary of original L/C.

6. Transferable Letter of Credit L/c: A transferable documentary credit is a type of credit under which the first beneficiary who is usually a middleman may request the nominated bank to transfer credit in whole or in part to the second beneficiary. The L/c clearly mentions the margins of the first beneficiary and unless it is specified the L/c cannot be treated as transferable. It can only be used when the company is selling the product of a third party. This type of L/c is used by companies acting as middle man during the transaction but not having large limit. The first beneficiary or middleman has rights to change the following terms and conditions of the letter of credit:

- Reduce the amount of the credit.
- Reduce unit price if it is stated

- Make shorter the expiry date of the letter of credit.
- Make shorter the last date for presentation of documents.
- Make shorter the period for shipment of goods.
- Increase the amount of the cover or percentage for which insurance cover must be effected.
- Substitute the name of the applicant (the middleman) for that of the first beneficiary (the buyer).

7. Standby Letter of Credit L/c: Initially used by the banks in the United States, the standby letter of credit is very much similar in nature to a bank guarantee. The main objective of issuing such a credit is to secure bank loans. Standby credits are usually issued by the applicant's bank in the applicant's country and advised to the beneficiary by a bank in the beneficiary's country. Unlike a traditional letter of credit where the beneficiary obtains payment against documents evidencing performance, the standby letter of credit allow a beneficiary to obtains payment from a bank even when the applicant for the credit has failed to perform as per bond. A standby letter of credit is subject to "Uniform Customs and Practice for Documentary Credit" (UCP), International Chamber of Commerce Publication No 500, 1993 Revision, or "International Standby Practices" (ISP), International Chamber of Commerce Publication No 590, 1998.

8. Red Clause Credit: The red clause L/C enables the beneficiary to draw a pre-determined value of the L/C as soon as it is established. The 'red clause' is an authority to the negotiating bank to make advances to the beneficiary for the purpose of purchasing the relevant goods.

9. Revolving credit: A revolving credit is designed to obviate the need for establishing new credit for each shipment when the transaction are more or less continuous. Under this provision may be made for making available the credit as soon as the importer reimburses the issuing bank with the drafts already negotiated by the paying bank.

EXPORT FINANCING

Financing international trade is a complex process, involving many variables, ranging from corporate policy and marketing strategy to exchange risk and general borrowing conditions. The reason behind the complexity of financing international trade is that trade involves two countries with different currencies and jurisdictions. In addition, payments must be made at a distance and across time, so the exporter, the importer, or both need credit during part or all of the period from the initial manufacture of goods by the exporting firm to the time of the final sale and collection by the importer.

The main objective of a good corporate export financing policy should be financing the greatest possible amount of sales with the greatest possible management simplicity and with minimal risk.

Following are among the important considerations in the choice of a strategy for trade financing:

- ***Nature of goods:*** Capital goods usually require medium to long-term financing while consumer goods, perishable products, etc. require short term finance.
- ***The nature of the relationship between the exporter and the importer.*** For example, if both are members of the same corporate family (affiliated to the same MNC) or have had a long standing relation with each other, the exporter may agree to sell on open account credit while absence of confidence may require a letter of credit.
- ***The availability of various forms of financing***, government regulations pertaining to the sale transaction, etc.

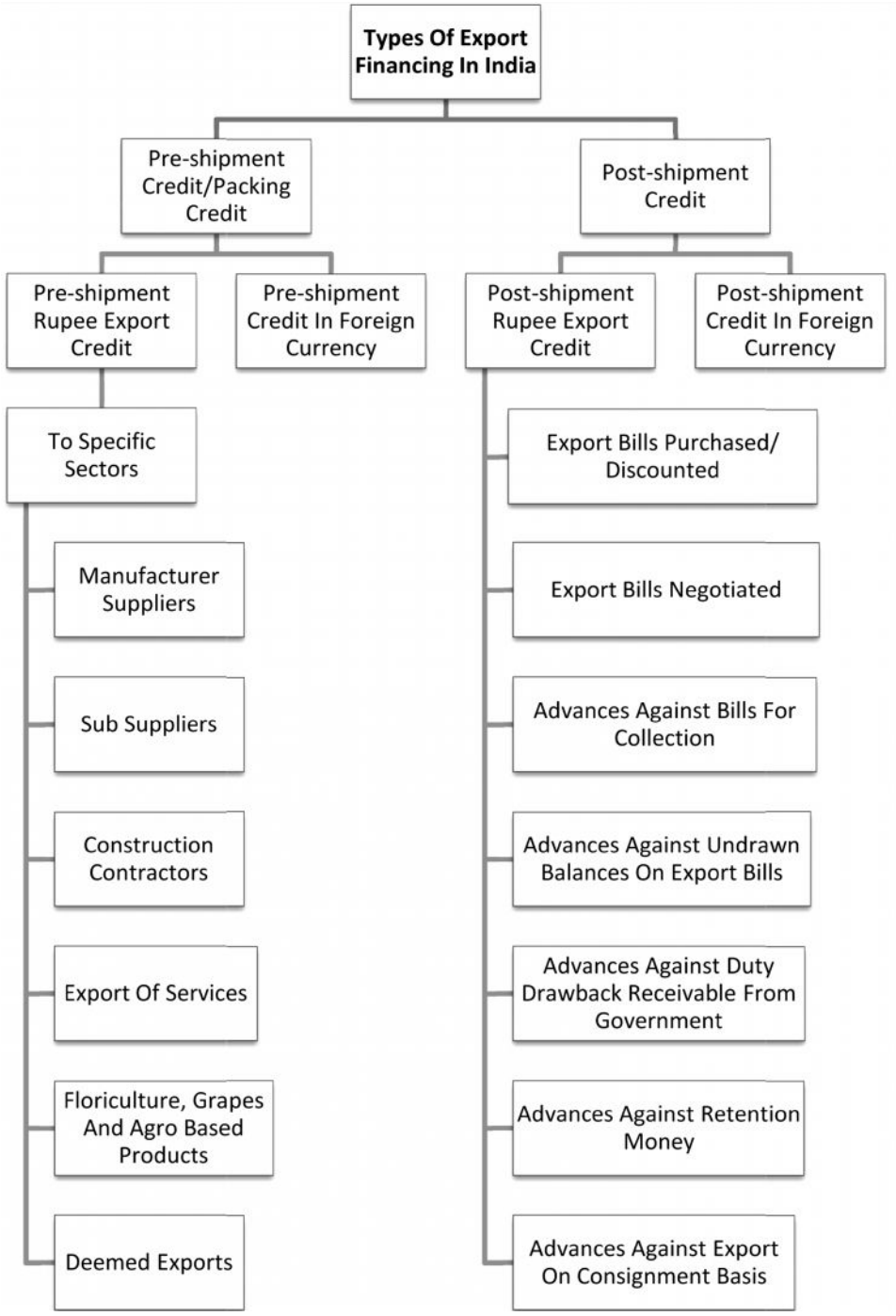
Companies often need financing to market, promote and manufacture their products and services. The financing needs of companies involved in international trade transactions are usually categorized as follows:

(a) Pre-shipment financing: this is financing for the period prior to the shipment of goods, to support pre-export activities, such as wages and overhead costs. It is especially needed when inputs for production must be imported. It also provides additional working capital for the exporter. Pre-shipment financing is especially important

to smaller enterprises because the international sales cycle is usually longer than the domestic sales cycle. Pre-shipment financing instruments can take the form of short-term loans, overdrafts or cash credits;

(b) Post-shipment financing: This is financing for the period following the shipment of goods. The competitiveness of exporters often depends on their ability to provide buyers with attractive credit terms. Post-shipment financing thus ensures adequate liquidity until the purchaser receives the products and the exporter receives payment. Post-shipment financing is usually short-term.

The RBI first introduced the scheme of Export Financing in 1967. The scheme is intended to make short-term working capital finance available to exporters at internationally comparable interest rates. RBI has issued the Master Circular dated July 1, 2011 consolidating the instructions / guidelines issued to banks till that date relating to Rupee / Foreign Currency Export Credit & Customer Service to Exporters.



PRE-SHIPMENT / PACKING CREDIT

Pre-shipment or Packing credit is a loan/ advance granted to an exporter for financing the purchase, processing, manufacturing or packing of goods prior to shipment. Packing credit can also be extended as working capital assistance to meet expenses such as wages, utility payments, travel expenses etc; to companies engaged in export or services. Packing credit is sanctioned/granted on the basis of letter of credit or a confirmed and irrevocable order for the export of goods / services from India or any other evidence of an order for export from India.

Pre Shipment Finance is issued by a financial institution when the seller wants the payment of the goods before shipment. The main objective behind preshipment finance or pre export finance is to enable exporter to:

- Procure raw materials.
- Carry out manufacturing process.
- Provide a secure warehouse for goods and raw materials.
- Process and pack the goods.
- Ship the goods to the buyers.
- Meet other financial cost of the business.

This facility is provided to an exporter who satisfies the following criteria

- A ten digit IEC number allotted by DGFT.
- Exporter should not be in the caution list of RBI.
- If the goods to be exported are not under OGL (Open General Licence), the exporter should have the required license /quota permit to export the goods.

Packing credit facility can be provided to an exporter on production of the following evidences to the bank:

- Formal application for release the packing credit with undertaking to the effect that the exporter would be ship the goods within stipulated due date and submit the relevant shipping documents to the banks within prescribed time limit.
- Firm order or irrevocable L/C or original cable / fax / telex message exchange between the exporter and the buyer.
- Licence issued by DGFT if the goods to be exported fall under the restricted or canalized category. If the item falls under quota system, proper quota allotment proof needs to be submitted.
- The confirmed order received from the overseas buyer should reveal the information about the full name and address of the overseas buyer, description quantity and value of goods (FOB or CIF), destination port and the last date of payment.

Pre shipment credit is only issued to that exporter who has the export order in his own name. However, as an exception, financial institution can also grant credit to a third party manufacturer or supplier of goods who does not have export orders in their own name.

In this case some of the responsibilities of meeting the export requirements have been out sourced to them by the main exporter. In other cases where the export order is divided between two more than two exporters, pre shipment credit can be shared between them.

The credit is granted to an exporter against the L/C or an expected order. The only guideline principle is the concept of NeedBased Finance. Banks determine the percentage of margin, depending on the natural of order, commodity & the capability of exporters to bring in the requisite contribution:

Stages of Granting Pre Shipment Credit to Exporter

1. Appraisal and Sanction of Limits: Before making any an allowance for Credit facilities banks need to check the different aspects like product profile, political and economic details about country. Apart from these things, the bank also looks in to the status report of the prospective buyer, with whom the exporter proposes to do the business. To check all these information, banks can seek the help of institutions like ECGC or International consulting agencies like Dun and Brad street etc. The Bank extends the packing credit facilities to exporters after ensuring –

- The exporter is a regular customer, a bona fide exporter and has a goods standing in the market.
- Whether the exporter has the necessary license and quota permit (as mentioned earlier) or not.
- Whether the country with which the exporter wants to deal is under the list of Restricted Cover Countries(RCC) or not.

2. Disbursement of Packing Credit Advance: Once the proper sanctioning of the documents is done, bank ensures whether exporter has executed the list of documents mentioned earlier or not. Disbursement is normally allowed when all the documents are properly executed. Sometimes an exporter is not able to produce the export order at time of availing packing credit. So, in these cases, the bank provide a special packing credit facility and is known as 'Running Account Facility'. Before disbursing the bank specifically check for the following particulars in the submitted documents

1. Name of buyer
2. Commodity to be exported
3. Quantity
4. Value (either CIF or FOB)
5. Last date of shipment / negotiation.
6. Any other terms to be complied with

The quantum of finance is fixed depending on the FOB value of contract /LC or the domestic values of goods, whichever is found to be lower. Normally insurance and freight charged are considered at a later stage, when the goods are ready to be shipped. Disbursals are made only in stages. The payments are made directly to the supplier by drafts/bankers' cheques. The bank decides the duration of packing credit depending upon the time required by the exporter for processing of goods. The maximum duration of packing credit period is 180 days, however bank may provide a further 90 days extension on its own discretion, without referring to RBI.

3. Follow up of Packing Credit Advance: Exporter needs to submit stock statement giving all the necessary information about the stocks. It is then used by the banks as a guarantee for securing the packing credit in advance. Apart from this, authorized dealers (banks) also physically inspect the stock at regular intervals.

4. Liquidation of Packing Credit Advance: The packing credit granted to an exporter may be liquidated out of proceeds of bills drawn for the exported commodities on its purchase, discount etc., thereby converting preshipment credit into post-shipment credit. This liquidation can also be done by the payment receivable from the Government of India and includes the duty drawback, payment from the Market Development Fund (MDF) of the Central Government or from any other relevant source. In case if the export does not take place then the entire advance can also be recovered at a certain interest rate. RBI has allowed some flexibility in to this regulation under which substitution of commodity or buyer can be allowed by a bank without any reference to RBI. Hence in effect the packing credit advance may be repaid by proceeds from export of the same or another commodity to the same or another buyer. However, bank need to ensure that the substitution is commercially necessary and unavoidable.

5. Overdue Packing: Bank considers a packing credit as an overdue, if the borrower fails to liquidate the packing credit on the due date. And, if the condition persists then the bank takes the necessary step to recover its dues as per normal recovery procedure.

TYPES OF PRE-SHIPMENT RUPEE EXPORT CREDIT

Rupee Export Packing Credit to Manufacturer Suppliers

Banks may grant export packing credit to manufacturer suppliers who do not have export orders/letters of credit in their own name and goods are exported through the State Trading Corporation/Minerals and Metal Trading Corporation or other export houses, agencies etc.

Rupee Export Packing Credit to Sub-Suppliers

Packing credit can be shared between an Export Order Holder (EOH) and sub-supplier of raw materials, components etc. of the exported goods as in the case of EOH and manufacturer suppliers.

- Packing Credit can only be shared on the basis of disclaimer between the Export Order Holder (EOH) and the manufacturer of the goods.
- This disclaimer is normally issued by the EOH in order to indicate that he is not availing any credit facility against the portion of the order transferred in the name of the manufacturer.
- This disclaimer is also signed by the bankers of EOH after which they have an option to open an inland L/C specifying the goods to be supplied to the EOH as a part of the export transaction.
- On basis of such an L/C, the sub-supplier bank may grant a packing credit to the subsupplier to manufacture the components required for exports.
- On supply of goods, the L/C opening bank will pay to the sub supplier's bank against the inland documents received on the basis of the inland L/C opened by them.
- The final responsibility of EOH is to export the goods as per guidelines. Any delay in export order can bring EOH to penal provisions that can be issued anytime.

The main objective of this method is to cover only the first stage of production cycles, and is not to be extended to cover supplies of raw material etc. Running account facility is not granted to subsuppliers. In case the EOH is a trading house, the facility is available commencing from the manufacturer to whom the order has been passed by the trading house. Banks however, ensure that there is no double financing and the total period of packing credit does not exceed the actual cycle of production of the commodity.

> ***What is Running Account facility:*** *It is a special facility under which a bank has right to grant preshipment advance for export to the exporter of any origin. Sometimes banks also extent these facilities depending upon the good track record of the exporter. In return the exporter needs to produce the letter of credit / firms export order within a given period of time.*

Rupee Pre-shipment Credit to Construction Contractors

The packing credit advances to the construction contractors to meet their initial working capital requirements for execution of contracts abroad may be made on the basis of a firm contract secured from abroad, in a separate account, on an undertaking obtained from them that the finance is required by them for incurring preliminary expenses in connection with the execution of the contract e.g., for transporting the necessary technical staff and purchase of consumable articles for the purpose of executing the contract abroad, etc.

Packing Credit facilities for Consulting Services

In case of consultancy services, exports do not involve physical movement of goods out of Indian Customs Territory. In such cases, Preshipment finance can be provided by the bank to allow the exporter to mobilize resources like technical personnel and training them.

Financing of Export of Services

Pre and post-shipment finance may be provided to exporters of all the 161 tradable services covered under the General Agreement on Trade in Services (GATS) where payment for such services is received in free foreign exchange as stated at Chapter 3 of the Foreign Trade Policy 2009-14. All provisions of this circular shall apply mutatis mutandis to export of services as they apply to export of goods unless otherwise specified. A list of services is given in Appendix 10 of HBPv1. The financing bank should ensure that there is no double financing and the export credit is liquidated with remittances from abroad. Banks may take into account the track record of the exporter/overseas counter party while sanctioning the export credit. The statement of export receivables from such service providers may be tallied with the statement of payables received from the overseas party.

Exporters of services qualify for working capital export credit (pre and post shipment) for consumables, wages, supplies etc. Banks may ensure that –

- *The proposal is a genuine case of export of services.*
- *The item of service export is covered under Appendix 10 of HBPv1.*
- *The exporter is registered with the Electronic and software EPC or Services EPC or with Federation of Indian Export Organisations, as applicable. There is an Export Contract for the export of the service.*
- *There is a time lag between the outlay of working capital expense and actual receipt of payment from the service consumer or his principal abroad.*
- *There is a valid Working Capital gap i.e. service is provided first while the payment is received some time after an invoice is raised.*
- *Banks should ensure that there is no double financing/excess financing.*
- *The export credit granted does not exceed the foreign exchange earned less the margins if any required, advance payment/credit received.*
- *Invoices are raised.*
- *Inward remittance is received in Foreign Exchange.*
- *Company will raise the invoice as per the contract. Where payment is received from overseas party, the service exporter would utilize the funds to repay the export credit availed of from the bank.*

Pre-shipment Credit to Floriculture, Grapes and Other Agro-based Products

(i) In the case of floriculture, pre-shipment credit is allowed to be extended by banks for purchase of cut-flowers etc. and all post-harvest expenses incurred for making shipment.

(ii) However, with a view to promoting export of floriculture, grapes and other agro-based products, banks are allowed to extend concessional credit for working capital purposes in respect of export-related activities of all agro-based products including purchase of fertilizers, pesticides and other inputs for growing of flowers, grapes etc., provided banks are in a position to clearly identify such activities as export-related and satisfy themselves of the export potential thereof, and that the activities are not covered by direct/indirect finance schemes of NABARD or any other agency, subject to the normal terms & conditions relating to packing credit such as period, quantum, liquidation etc.

(iii) Export credit should not be extended for investments, such as, import of foreign technology, equipment, land development etc. or any other item which cannot be regarded as working capital.

Packing Credit Facilities to Deemed Exports

Deemed exports made to multilateral funds aided projects and programmes, under orders secured through global tenders for which payments will be made in free foreign exchange, are eligible for concessional rate of interest facility both at pre and post supply stages.

PRE-SHIPMENT CREDIT IN FOREIGN CURRENCY (PCFC)

With a view to making credit available to exporters at internationally competitive rates, authorised dealers have been permitted to extend pre-shipment Credit in Foreign Currency (PCFC) to exporters for domestic and imported inputs of exported goods at LIBOR/EURO LIBOR/EURIBOR related rates of interes*t. The scheme is an additional window for providing pre-shipment credit to Indian exporters at internationally* competitive rates of interest. It will be applicable to only cash exports. The instructions with regard to Rupee Export Credit apply to export credit in Foreign Currency also mutatis mutandis, unless otherwise specified.

The exporter will have the following options to avail of export finance:

(a) to avail of pre-shipment credit in rupees and then the post-shipment credit either in rupees or discounting/ rediscounting of export bills under EBR Scheme

(b) to avail of pre-shipment credit in foreign currency and discount/ rediscounting of the export bills in foreign currency under EBR Scheme.

(c) to avail of pre-shipment credit in rupees and then convert drawals into PCFC at the discretion of the bank.

Choice of currency

(a) The facility may be extended in one of the convertible currencies viz. US Dollars, Pound Sterling, Japanese Yen, Euro, etc.

(b) To enable the exporters to have operational flexibility, it will be in order for banks to extend PCFC in one convertible currency in respect of an export order invoiced in another convertible currency. *For example*, an exporter can avail of PCFC in US Dollar against an export order invoiced in Euro. The risk and cost of cross currency transaction will be that of the exporter.

(c) Banks are permitted to extend PCFC for exports to ACU countries.

(d) The applicable benefit to the exporters will accrue only after the realisation of the export bills or when the resultant export bills are rediscounted on 'without recourse' basis.

- Authorised dealers are permitted to extend Preshipment Credit in Foreign Currency (PCFC) with an objective of making the credit available to the exporters at internationally competitive price.
- This is considered as an added advantage under which credit is provided in foreign currency in order to facilitate the purchase of raw material after fulfilling the basic export orders.
- The rate of interest on PCFC is linked to London Interbank Offered Rate (LIBOR).
- According to guidelines, the final cost of exporter must not exceed 0.75% over 6 month LIBOR, excluding the tax.
- The exporter has freedom to avail PCFC in convertible currencies like USD, Pound, Sterling, Euro, Yen etc.
- The sources of funds for the banks for extending PCFC facility include the Foreign Currency balances available with the Bank in Exchange, Earner Foreign Currency Account (EEFC), Resident Foreign Currency Accounts RFC(D) and Foreign Currency(NonResident) Accounts.
- Banks are also permitted to utilize the foreign currency balances available under Escrow account and Exporters Foreign Currency accounts. It ensures that the requirement of funds by the account holders for permissible transactions is met. But the limit prescribed for maintaining maximum balance in the account is not exceeded. In addition, Banks may arrange for borrowings from abroad.
- Banks may negotiate terms of credit with overseas bank for the purpose of grant of PCFC to exporters,

without the prior approval of RBI, provided the rate of interest on borrowing does not exceed 0.75% over 6 month LIBOR.

'POST-SHIPMENT CREDIT'

'Post-shipment Credit' means any loan or advance granted or any other credit provided by a bank to an exporter of goods / services from India from the date of extending credit after shipment of goods / rendering of services to the date of realisation of export proceeds as per the period of realization prescribed by Reserve Bank of India (RBI) and includes any loan or advance granted to an exporter, in consideration of, or on the security of any duty drawback allowed by the Government from time to time. As per extant guidelines of RBI, the period prescribed for realisation of export proceeds is 12 months from the date of shipment.

Post Shipment Credit is a kind of loan provided by a financial institution to an exporter or seller against a shipment that has already been made. This type of export finance is granted from the date of extending the credit after shipment of the goods to the realization date of the exporter proceeds. Exporters don't wait for the importer to deposit the funds.

It is meant to finance export sales receivable after the date of shipment of goods to the date of realization of exports proceeds. In cases of deemed exports, it is extended to finance receivable against supplies made to designated agencies.

Post shipment finances are provided against evidence of shipment of goods or supplies made to the importer or seller or any other designated agency.

*P*ost shipment finance can be extended up to 100% of the invoice value of goods. In special cases, where the domestic value of the goods increases the value of the exporter order, finance for a price difference can also be extended and the price difference is covered by the government. This type of finance is not extended in case of pre shipment stage. Banks can also finance undrawn balance. In such cases banks are free to stipulate margin requirements as per their usual lending norm.

Post shipment finance can be off short terms or long term, depending on the payment terms offered by the exporter to the overseas importer. In case of cash exports, the maximum period allowed for realization of exports proceeds is six months from the date of shipment. Concessive rate of interest is available for a highest period of 180 days, opening from the date of surrender of documents. Usually, the documents need to be submitted within 21days from the date of shipment.

TYPES OF POST SHIPMENT RUPEE EXPORT CREDIT

Export Bills Purchased/ Discounted (DP & DA Bills)

Export bills (Non L/C Bills) is used in terms of sale contract/ order may be discounted or purchased by the banks. It is used in indisputable international trade transactions and the proper limit has to be sanctioned to the exporter for purchase of export bill facility.

Export Bills Negotiated (Bill under L/C)

The risk of payment is less under the L/C, as the issuing bank guarantees the payment. The risk is further reduced, if a bank guarantees the payments by confirming the L/C. Because of the security available in this method, banks often become ready to extend the finance against bills under L/C. However, these are two major risk factors for the banks:

1. The risk of nonperformance by the exporter, when he is unable to meet his terms and conditions. In this case, the issuing banks do not honor the letter of credit.
2. The bank also faces the documentary risk where the issuing bank refuses to honour its commitment. So, it is important for the for the negotiating bank, and the lending bank to properly check all the necessary documents before submission.

Advance against bills for collection

Post-shipment credit is to be liquidated by the proceeds of export bills received from abroad in respect of goods exported / services rendered. Further, subject to mutual agreement between the exporter and the banker it can also be repaid / prepaid out of balances in Exchange Earners Foreign Currency Account (EEFC A/C) as also from proceeds of any other unfinanced (collection) bills.

In order to reduce the cost to exporters (i.e. interest cost on overdue export bills), exporters with overdue export bills may also extinguish their overdue post shipment rupee export credit from their rupee resources.

Advances against Undrawn Balances on Export Bills

In respect of export of certain commodities where exporters are required to draw the bills on the overseas buyer up to 90 to 98 percent of the FOB value of the contract, the residuary amount being 'undrawn balance' is payable by the overseas buyer after satisfying himself about the quality/ quantity of goods.

Payment of undrawn balance is contingent in nature. Banks may consider granting advances against undrawn balances at concessional rate of interest based on their commercial judgement and the track record of the buyer. Such advances are, however, eligible for concessional rate of interest for a maximum period of 90 days only to the extent these are repaid by actual remittances from abroad and provided such remittances are received within 180 days after the expiry of NTP in the case of demand bills and due date in the case of usance bills. For the period beyond 90 days, the rate of interest specified for the category 'ECNOS' at post-shipment stage may be charged.

Post-shipment Advances against Duty Drawback Entitlements

Banks may grant post-shipment advances to exporters against their duty drawback entitlements and covered by ECGC guarantee as provisionally certified by Customs Authorities pending final sanction and payment.

The advance against duty drawback receivables can also be made available to exporters against export promotion copy of the shipping bill containing the EGM Number issued by the Customs Department. Where necessary, the financing bank may have its lien noted with the designated bank and arrangements may be made with the designated bank to transfer funds to the financing bank as and when duty drawback is credited by the Customs.

These advances granted against duty drawback entitlements would be eligible for concessional rate of interest and refinance from RBI up to a maximum period of 90 days from the date of advance.

Advances against Retention Money

In the case of turnkey projects/construction contracts, progressive payments are made by the overseas employer in respect of services segment of the contract, retaining a small percentage of the progressive payments as retention money which is payable after expiry of the stipulated period from the date of the completion of the contract, subject to obtention of certificate(s) from the specified authority. Retention money may also be sometimes stipulated against the supplies portion in the case of turn-key projects. It may like-wise arise in the case of sub-contracts. The payment of retention money is contingent in nature as it is a defect liability.

Advance against export on consignment basis

Export on consignment basis lends scope for a lot of misuse in the matter of repatriation of export proceeds. Therefore, export on consignment basis should be at par with exports on outright sale basis on cash terms in matters regarding the rate of interest to be charged by banks on post-shipment credit. Thus, in the case of exports on consignment basis, even if extension in the period beyond 365 days is granted by the Foreign Exchange Department (FED) for repatriation of export proceeds, banks will charge appropriate prescribed rate of interest only up to the notional due date (depending upon the tenor of the bills), subject to a maximum of 365 days.

POST-SHIPMENT CREDIT IN FOREIGN CURRENCY

This credit is provided under Rediscounting of Export Bills Abroad Scheme (EBR). Banks may utilise the foreign exchange resources available with them in Exchange Earners Foreign Currency Accounts (EEFC), Resident Foreign Currency Accounts (RFC), Foreign Currency (Non-Resident) Accounts (Banks) Scheme, to discount usance bills and retain them in their portfolio without resorting to rediscounting. Banks are also allowed to rediscount export bills abroad at rates linked to international interest rates at post-shipment stage.

It will be comparatively easier to have a facility against bills portfolio (covering all eligible bills) than to have rediscounting facility abroad on bill by bill basis. There will, however, be no bar if rediscounting facility on bill to bill basis is arranged by a bank in case of any particular exporter, especially for large value transactions.

Banks may arrange a **"Bankers Acceptance Facility" (BAF)** for rediscounting the export bills without any margin and duly covered by collateralised documents.

Each bank can have its own BAF limit(s) fixed with an overseas bank or a rediscounting agency or an arrangement with any other agency such as factoring agency (in case of factoring arrangement, it should be on 'without recourse' basis only).

The exporters, on their own, can arrange for themselves a line of credit with an overseas bank or any other agency (including a factoring agency) for discounting their export bills direct subject to the following conditions:

- Direct discounting of export bills by exporters with overseas bank and/or any other agency will be done only through the branch of an authorized dealer designated by him for this purpose.
- Discounting of export bills will be routed through designated bank / authorized dealer from whom the packing credit facility has been availed of. In case, these are routed through any other bank, the latter will first arrange to adjust the amount outstanding under packing credit with the concerned bank out of the proceeds of the rediscounted bills.

The limits granted to banks by overseas banks/discounting agencies under BAF will not be reckoned for the purpose of borrowing limits fixed by RBI (FED) for them.

Eligibility Criteria

- The Scheme will cover mainly export bills with usance period up to 180 days from the date of shipment (inclusive of normal transit period and grace period, if any). There is, however, no bar to include demand bills, if overseas institution has no objection to it.
- In case borrower is eligible to draw usance bills for periods exceeding 180 days as per the extant instructions of FED, Post-shipment Credit under the EBR may be provided beyond 180 days.
- The facility under the Scheme of Rediscounting may be offered in any convertible currency.
- Banks are permitted to extend the EBR facility for exports to ACU countries.

  For operational convenience, the BAF Scheme may be centralised at a branch designated by the bank. There will, however, be no bar for other branches of the bank to operate the scheme as per the bank's internal guidelines / instructions.

FACTORING AND FORFAITING

The terms factoring and forfaiting have been mixed up frequently. Factoring is suitable for financing several and different smaller claims for consumer goods with credit terms between 90 and 180 days, whereas forfaiting is used to finance capital goods exports with credit terms between a few months and seven years. Factoring only covers the commercial risk, whereas forfaiting additionally covers the political and transfer risk.

EXPORT FACTORING

Export factoring is a complete financial package that combines export working capital financing, credit protection, foreign accounts receivable bookkeeping, and collection services. A factoring house, or factor, is a bank or specialized financial firm that performs financing through the purchase of invoices or accounts receivable. Export factoring is offered under an agreement between the factor and exporter, in which the factor purchases the exporter's short-term foreign accounts receivable for cash at a discount from the face value, normally without recourse. It also assumes the risk on the ability of the foreign buyer to pay, and handles collections on the receivables. Thus, by virtually eliminating the risk of non-payment by foreign buyers, factoring allows the exporter to offer open accounts, improves liquidity position, and boosts competitiveness in the global marketplace. Factoring foreign accounts receivables can be a viable alternative to export credit insurance, long-term bank financing, expensive short-term bridge loans or other types of borrowing that create debt on the balance sheet.

– It is ideal for an established exporter who wants

(a) to have the flexibility to sell on open account terms,

(b) to avoid incurring any credit losses, or

(c) to outsource credit and collection functions.

– Factoring is recommended for continuous short-term export sales of consumer goods on open accounts.

– It offers 100 percent protection against the foreign buyer's inability to pay — with no deductible or risk sharing.

– It is an attractive option for small and medium-sized exporters, particularly during periods of rapid growth, because cash flow is preserved and risk is virtually eliminated.

– It is unsuitable for the new-to-export company as factors generally

(d) do not take on a client for a onetime deal and

(e) require access to a certain volume of the exporter's yearly sales.

– It eliminates the risk of non-payment by foreign buyers and maximizes cash flows.

How Does Export Factoring Work?

– The exporter signs an agreement with the export factor who selects an import factor through an international correspondent factor network, who then investigates the foreign buyer's credit standing.

– Once credit is approved locally, the foreign buyer places orders for goods on open account.

– The exporter then ships the goods and submits the invoice to the export factor, who then passes it to the import factor.

– The import factor then handles the local collection and payment of the accounts receivable. During all stages of the transaction, records are kept for the exporter's bookkeeping.

Different Types of Factoring

1. Disclosed: In disclosed factoring, client's customers are aware of the factoring agreement. Disclosed factoring is of two types:

***(a) Recourse factoring*:** The client collects the money from the customer but in case customer don't pay the amount on maturity then the client is responsible to pay the amount to the factor. It is offered at a low rate of interest and is in very common use.

(b) Nonrecourse factoring: In nonrecourse factoring, factor undertakes to collect the debts from the customer. Balance amount is paid to client at the end of the credit period or when the customer pays the factor whichever comes first. The advantage of nonrecourse factoring is that continuous factoring will eliminate the need for credit and collection departments in the organization.

2. Undisclosed: In undisclosed factoring, client's customers are not notified of the factoring arrangement. In this case, Client has to pay the amount to the factor irrespective of whether customer has paid or not.

Limitations of Export Factoring

- It exists in countries with laws that support the buying and selling of receivables.
- It generally does not work with foreign account receivables that have more than 180-day terms.
- It may be cost prohibitive for exporters with tight profit margins.
- It is more costly than export credit insurance

FORFAITING

Forfaiting is the term generally used to denote the purchase of obligations falling due at some future date, arising from deliveries of goods and services - mostly export transactions - without recourse to any previous holder of the obligation. The forfaiter will deduct interest (discount) in advance for the whole period of credit and disburse the net proceeds immediately. The exporter thus virtually converts his credit based sale into a cash transaction. His sole responsibilities are manufacturing and delivery of the goods, thus creating a valid payment obligation of the importer.

Forfaiting is a method of trade finance that allows exporters to obtain cash by selling their medium-term foreign accounts receivable at a discount on a "without recourse" basis.

A forfaiter is a specialized finance firm or a department in a bank that performs non-recourse export financing through the purchase of medium-term trade receivables.

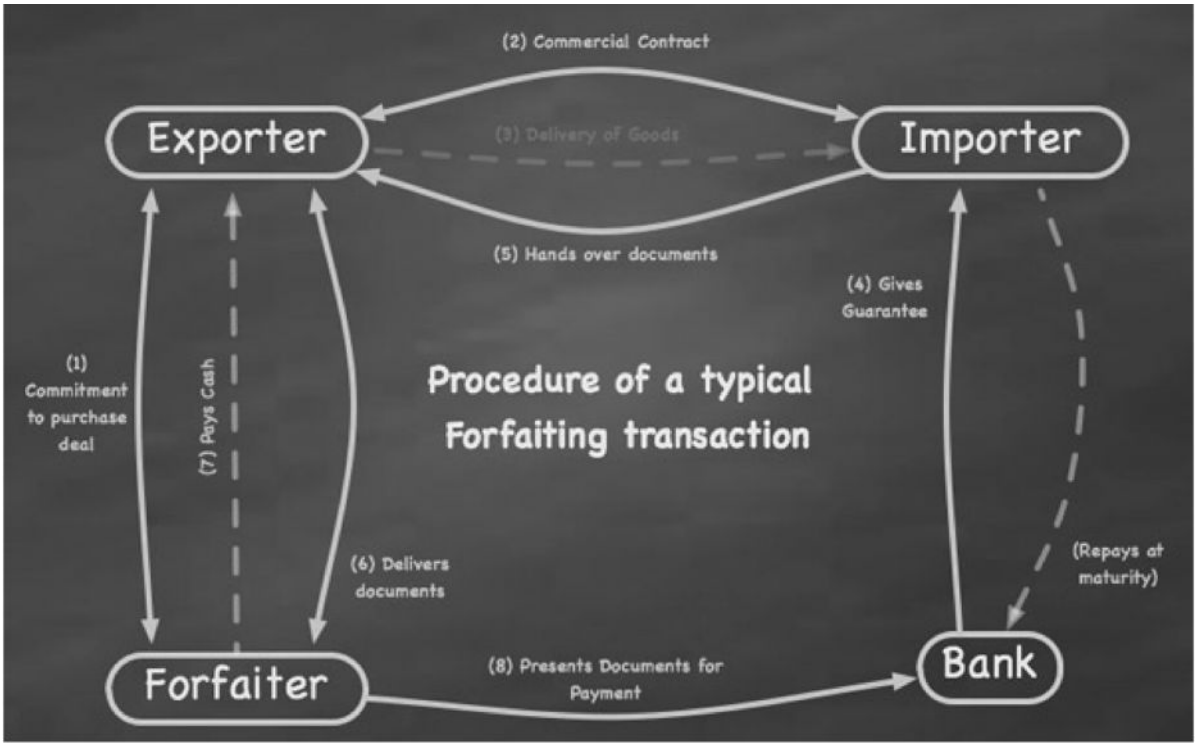
Similar to factoring, forfaiting virtually eliminates the risk of non-payment, once the goods have been delivered to the foreign buyer in accordance with the terms of sale. However, unlike factors, forfaiters typically work with exporters who sell capital goods, commodities, or large projects and needs to offer periods of credit from 180 days to seven years.

In forfaiting, receivables are normally guaranteed by the importer's bank, which allows the exporter to take the transaction off the balance sheet to enhance key financial ratios.

- Forfaiting eliminates virtually all risk to the exporter, with 100 percent financing of contract value.
- Exporters can offer medium-term financing in markets where the credit risk would otherwise be too high.
- Forfaiting generally works with bills of exchange, promissory notes, or a letter of credit.
- The exporter is normally required to obtain a bank guarantee for the foreign buyer.
- Financing can be arranged on a one-shot basis in any of the major currencies, usually at a fixed interest rate, but a floating rate option is also available.
- Forfaiting can be used in conjunction with officially supported credits backed by export credit agencies.
- It is ideal for exports of capital goods, commodities, and large projects on medium-term credit (180 days to seven years).
- Cost of forfaiting is often higher than commercial lender financing

How Forfaiting Works

- The exporter approaches a forfaiter before finalizing a transaction's structure.
- Once the forfaiter commits to the deal and sets the discount rate, the exporter can incorporate the discount into the selling price.
- The exporter then accepts a commitment issued by the forfaiter, signs the contract with the importer, and obtains, if required, a guarantee from the importer's bank that provides the documents required to complete the forfaiting.
- The exporter delivers the goods to the importer and delivers the documents to the forfaiter who verifies them and pays for them as agreed in the commitment.
- Since this payment is without recourse, the exporter has no further interest in the transaction and it is the forfaiter who must collect the future payments due from the importer.



In case of Indian exporters availing forfaiting facility, the forfeiting transaction is to be reflected in the following documents associated with an export transaction in the manner suggested below:

- **Invoice** : Forfaiting discount, commitment fees, etc. needs not be shown separately instead, these could be built into the FOB price, stated on the invoice.
- **Shipping Bill and GR form :** Details of the forfeiting costs are to be included along with the other details, such FOB price, commission insurance, normally included in the "Analysis of Export Value "on the shipping bill. The claim for duty drawback, if any is to be certified only with reference to the FOB value of the exports stated on the shipping bill.

The forfaiting typically involves the following cost elements:

- Commitment fee, payable by the exporter to the forfeiter 'for latter's' commitment to execute a specific forfeiting transaction at a firm discount rate with in a specified time.

– Discount fee, interest payable by the exporter for the entire period of credit involved and deducted by the forfaiter from the amount paid to the exporter against the availised promissory notes or bills of exchange.

Benefits to Exporter

– **100 per cent financing** : Without recourse and not occupying exporter's credit line That is to say once the exporter obtains the financed fund, he will be exempted from the responsibility to repay the debt.

– **Improved cash flow** : Receivables become current cash in flow and its is beneficial to the exporters to improve financial status and liquidation ability so as to heighten further the funds raising capability.

– **Reduced administration cost** : By using forfeiting , the exporter will spare from the management of the receivables. The relative costs, as a result, are reduced greatly.

– **Advance tax refund**: Through forfeiting the exporter can make the verification of export and get tax refund in advance just after financing.

– **Risk reduction** : forfeiting business enables the exporter to transfer various risk resulted from deferred payments, such as interest rate risk, currency risk, credit risk, and political risk to the forfeiting bank.

– **Increased trade opportunity** : With forfeiting, the export is able to grant credit to his buyers freely, and thus, be more competitive in the market.

Benefits to Banks

Forfeiting provides the banks following benefits:

– Banks can offer a novel product range to clients, which enable the client to gain 100% finance, as against 8085% in case of other discounting products.

– Bank gain fee based income.

– Lower credit administration and credit follow up.

QUALITY CONTROL & PRE SHIPMENT INSPECTION

An important aspect about the goods to be exported is compulsory quality control and pre-shipment inspection. For this purpose, Export Inspection Council (EIC) was set up by the Government of India under Section 3 of the Export (Quality Control and Inspection) Act, 1963. It includes more than 1000 commodities which are organised into various groups for a compulsory pre-shipment inspection. It includes Food and Agriculture, Fishery, Minerals, Organic and Inorganic Chemicals, Rubber Products, Refractoriness, Ceramic Products, Pesticides, Light Engineering, Steel Products, Jute Products, Coir and Coir and Coir Products, Footwear and Footwear Products.

Sometimes overseas buyers lay their own standards/specifications which may or may not be in consonance with the Indian standards. They may also insist upon inspection by their own nominated agencies. These issues should be sorted out before confirmation of order.

Specific provision have also been made for compulsory inspection of textile goods. Products having ISI Certification mark or Agmark are not required to be inspected by any agency. These products do not fall within the purview of the export inspection agencies network. The Customs Authorities allow shipment of such goods without inspection certificate, provided they are otherwise satisfied that the goods carry ISI Certification Mark or the Agmark. For other goods inspection can be made in the following manner:

Procedure for pre-shipment inspection : Under the Consignment to consignment inspection scheme' the application (in duplicate) for inspection for goods has to be submitted well in advance, in the new prescribed form 'intimation for inspection', before the expected date of shipment of the consignment.

Inspection of the consignment is generally carried out either at the premises of the exporter, provided adequate facilities exist therein for inspection, or at the port of shipment.

After satisfying itself that the consignment of exportable goods meets the requirements stipulated in the export contract/order, the inspection agency issues, generally within four days of receipt of intimation for inspection, the necessary certificate of inspection to the exporter in the prescribed proforma in five copies.

The certificate is issued in the standardised form which is aligned pre-shipment export document. (Three copies for exporter, original copy for customs use, the second copy for the use of the foreign buyer and the third copy for the exporter's use, fourth copy for Data Bank, Export Inspection Council, New Delhi and the fifth copy is retained with the agency for their own office record).

Documents required for quality control & preshipment inspection

There are certain forms and documents that are necessary for quality control and pre-shipment inspection. The following documents need to be submitted along with the application:

- Particulars of the consignment intended to be exported
- A crossed cheque/draft for the amount of requisite inspection fees or an Indian Postal Order.
- Copy of commercial invoice
- Copy of Letter of Credit
- Details of packing specifications
- Copy of the export order/contract, indicating inter alia the buyer's requirement that goods are strictly according to the prescribed specifications or as per samples

ISI Certification

Indian Standards Institute now known as Bureau of Indian Standard (BIS) is a registered society under a Government of India. BIS main functions include the development of technical standards, product quality and management system certifications and consumer affairs. Founded by Professor P.C. Mahalanobis in Kolkata on 17th December, 1931, the institute gained the status of an Institution of National Importance by an act of the Indian Parliament in 1959.

AgMark Certification

AgMark is an acronym for Agricultural Marketing and is used to certify the food products for quality control. Agmark has been dominated by other quality standards including the non manufacturing standard ISO 9000.

Benefits of ISI and Agmark Certification

Products having ISI Certification mark or Agmark are not required to be inspected by any agency. These products do not fall within the purview of the export inspection agencies network. The Customs Authorities allow export of such goods even if not accompanied by any pre-shipment inspection certificate, provided they are otherwise satisfied that the goods carry ISI Certification or the Agmark.

In-process Quality Control (IPQC):

Certain products like chemicals or engineering goods are subject to this control. The inspection is done at various

stages of production. The exporter has to get his unit registered as "Export worthy" and keep record of processing and production. Under this system, export is allowed on the basis of adequacy of IPQC and inspection measures exercised by the manufacturing units themselves. Units approved under this system may themselves issue the certificate of inspection, but only for the products for which they have been granted IPQC facilities. However, these units have the option either to get the certificate from the export inspection agencies (EIAs) or issue the same themselves. In-Process Quality Control (IPQC) inspection is mainly done for engineering products and is applied at the various stages of production. Units approved under IPQC system of in-process quality control may themselves issue the certificate of inspection, but only for the products for which they have been granted IPQC facilities. The final certificate of inspection on the end-products is then given without in-depth study at the shipment stage.

Self-certification Scheme

Large manufacturing/exporters, export houses/trading houses are allowed the facility of self-certification on the theory that the exporter himself is the best judge of the quality of his products.

The industrial units having proven reputation and adequate testing facilities have to apply to the Director (Inspection and Quality Control), Export Inspection Council of India, 11th floor, Pragati Tower, 26 Rajendra Place, New Delhi-110 008. It grants a certificate valid for a period of one year, to allow manufacturers of engineering products, chemical and allied products and marine products. The approval of an industrial unit under this scheme is notified in the Gazette of India and the exporter has to pay a lump sum fee to the export inspection agencies depending upon his export turnover.

Discussion on Quality Control and preshipment inspection will be incomplete without saying a few words about ISO 9000. The International Organisation for Standardisation (ISO) is the specialised International Agency in formulating the norms of Standardisation, Presently 91 Countries including India are members of the national Standard Body Various Technical Committees were formed who looked into and considered the different areas of specialisation and formulated the International Standard.

ISO 9000

The discussion on inspection certificate and quality control is incomplete without ISO-9000. Established in 1987, ISO 9000 is a series of international standards that has been accepted worldwide as the norm assuring high quality of goods. The current version of ISO 9000 is ISO 9000:2000.

PACKING AND LABELING OF GOODS

An important stage after manufacturing of goods or their procurement is their preparation for shipment which involves packaging and labelling of goods to be exported. Proper packaging and labelling not only makes the final product look attractive but also save a huge amount of money by saving the product from wrong handling the export process.

Packaging

The primary role of packaging is to contain, protect and preserve a product as well as aid in its handling and final presentation. Packaging also refers to the process of design, evaluation, and production of packages. The packaging can be done within the export company or the job can be assigned to an outside packaging company. Packaging provides following benefits to the goods to be exported:

- **Physical Protection** : Packaging provides protection against shock, vibration, temperature, moisture and dust.
- **Containment or agglomeration** : Packaging provides agglomeration of small objects into one package for reason of efficiency and cost factor. For example it is better to put 1000 pencils in one box rather than putting each pencil in separate 1000 boxes.
- **Marketing** : Proper and attractive packaging play an important role in encouraging a potential buyer.
- **Convenience** : Packages can have features which add convenience in distribution, handling, display, sale, opening, use, and reuse.

– **Security** : Packaging can play an important role in reducing the security risks of shipment. It also provides authentication seals to indicate that the package and contents are not counterfeit. Packages also can include anti-theft devices, such as dye-packs, RFID tags, or electronic article surveillance tags, that can be activated or detected by devices at exit points and require specialized tools to deactivate. Using packaging in this way is a means of loss prevention.

Labeling

Like packaging, labeling should also be done with extra care. It is also important for an exporter to be familiar with all kinds of sign and symbols and should also maintain all the nationally and internationally standers while using these symbols. Labelling should be in English, and words indicating country of origin should be as large and as prominent as any other English wording on the package or label. Labelling on product provides the following important information:

– Shipper's mark

– Country of origin

– Weight marking (in pounds and in kilograms)

– Number of packages and size of cases (in inches and centimeters)

– Handling marks (international pictorial symbols)

– Cautionary markings, such as "This Side Up."

– Port of entry

– Labels for hazardous materials

Labelling of a product also provides information like how to use, transport, recycle, or dispose of the package or product. With pharmaceuticals, food, medical, and chemical products, some types of information are required by governments. It is better to choose a fast dyes for labelling purpose. Only fast dyes should be used for labeling. Essential data should be in black and subsidiary data in a less conspicuous colour; red and orange and so on. For food packed in sacks, only harmless dyes should be employed, and the dye should not come through the packing in such a way as to affect the goods.

CENTRAL EXCISE CLEARANCE PROCEDURE FOR EXPORT

As a part of further simplifications and rationalisation of excise rules announced by the Finance Minister, a set of Central Excise Rules, 2002 has come into effect from 1-3-2002. Under these new rules, central excise provisions for exports (except exports to Nepal and Bhutan) have been prescribed in Rule 18 and 19.

PROCEDURE FOR EXPORT TO ALL COUNTRIES (EXCEPT NEPAL AND BHUTAN) UNDER PAYMENT OF DUTY

The procedure for export of excisable goods except Nepal and Bhutan on payment of duty under claim for rebate is governed by the provisions of Rule 18 of the Central Excise (No.2) Rules, 2001. The conditions, limitations and safeguards are separately contained in Notification No. 40/2001-CE(NT) dated 26''' June, 2001.

Conditions and Limitations –

(i) that the excisable goods shall be exported after payment of duty, directly from a factory or warehouse;

(ii) the excisable goods shall be exported within six months from the date on which they were, cleared for export, from the factory of manufacture or warehouse;

(iii) the rebate claim by filing electronic declaration shall be allowed from such place of export and such date, as may be specified by the Board in this behalf;

(iv) that the market price of the excisable goods at the time of exportation is not less than the amount of rebate of duty claimed;

(v) that the amount of rebate of duty admissible is not less than five hundred rupees.

Sealing of goods and examination at place of dispatch

(a) For the sealing of goods intended for export at the place of despatch, the exporter shall present the goods along with four copies of application in the Form ARE-I to the Superintendent or Inspector of Central Excise having jurisdiction over the factory of production or manufacture or warehouse, who will verify the identity of goods mentioned in the application and the particulars of the duty paid or payable, and if found in order, he shall seal each package or the container in the manner as may be specified by the Commissioner of Central Excise and endorse each copy of the application in token of having such examination done;

(b) The said Superintendent or Inspector of Central Excise shall return the original and duplicate copies of application to the exporter.

(c) The triplicate copy of application shall be, —

– sent to the officer with whom rebate claim is to be filed, either by post or by handing over to the exporter in a tamper proof sealed cover after posting the particulars in official records, or

– Sent to the Excise Rebate Audit Section at the place of export in case rebate is to be claimed by electronic declaration on Electronic Data Inter¬change system of Customs.

(d) The exporter may prepare quintuplicate copy of application for claiming any other export incentive. This copy shall be dealt in the same manner as the original copy of application.

(e) where goods are not exported directly from the factory of manufacture or warehouse, the triplicate copy of application shall be sent by the Superintendent having jurisdiction over the factory of manufacture or warehouse who shall, after verification forward the triplicate copy in the manner specified in sub-paragraph (c) above.

Despatch of goods by self-sealing and self-certification

(a) Where the exporter desires self-sealing and self-certification for removal of goods from the factory or warehouse, the exporter or a person duly authorised by such exporter, shall certify on all the copies of the application that the goods have been sealed in his presence, and shall send the original and duplicate copies of the application along with the goods at the place of export, and shall send the triplicate and quadruplicate copies of the application to the Superintendent or Inspector of Central Excise having jurisdiction over the factory or warehouse within twenty four hours of removal of the goods.

(b) The said Superintendent or Inspector of Central Excise shall, after verifying the particulars of the duty paid or duty payable and endorsing the correctness or otherwise, of these particulars

– send to the officer with whom rebate claim is to be filed, either by post or by handing over to the exporter in a tamper proof sealed cover after posting the particulars in official records, or

– send to the Excise Rebate Audit Section at the place of export in case rebate is to be claimed by electronic declaration on Electronic Data Inter¬change system of Customs.

(c) The exporter may prepare quintuplicate copy of application for claiming any other export incentive. This copy shall be dealt in the same manner as the original copy of application.

Examination of goods at the place of export

(a) On arrival at the place of export, the goods shall be presented together with original, duplicate and

quintuplicate (optional) copies of the application to the Commissioner of Customs or other duly appointed officer;

(b) The Commissioner of Customs or other duly appointed officer shall examine the consignments with the particulars as cited in the application and if he finds that the same are correct and exportable in accordance with the laws for the time being in force, shall allow export thereof and certify on the copies of the application that the goods have been duly exported citing the shipping bill number and date and other particulars of export,

(c) Provided that if the Superintendent or Inspector of Central Excise has sealed packages or container at the place of despatch, the officer of customs shall inspect the packages or container with reference to declarations in the application to satisfy himself about the exportability thereof and if the seals are found intact, he shall allow export.

(d) The officer of customs shall return the original and quintuplicate (optional copy for exporter) copies of application to the exporter and forward the duplicate copy of application either by post or by handing over to the exporter in a tamper proof sealed cover to the officer specified in the application, from whom exporter wants to claim rebate,

(e) Provided that where exporter claims rebate by electronic declaration on Electronic Data Inter-change system of Customs, the duplicate shall be sent to the Excise Rebate Audit Section at the place of export.

(f) The exporter shall use the quintuplicate copy for the purposes of claiming any other export incentive;

Presentation of claim for rebate to Central Excise

(a) Claim of the rebate of duty shall be lodged along with original copy of the application to the Assistant Commissioner of Central Excise or the Deputy Commissioner of Central Excise having jurisdiction over the factory of manufacture or warehouse or, as the case may be, the Maritime Commissioner;

(b) The Assistant Commissioner of Central Excise or the Deputy Commissioner of Central Excise having jurisdiction over the factory of manufacture or warehouse or, as the case may be, Maritime Commissioner of Central Excise shall compare the duplicate copy of application received from the Officer of Customs with the original copy received from the exporter and with the triplicate copy received from the Central Excise Officer and if satisfied that the claim is in order, he shall sanction the rebate either in whole or in part.

Claim of rebate by electronic declaration

An exporter may enter the requisite information in the Shipping Bill filed at such place of export, as may be specified by the Board, for claiming rebate by electronic declaration on Electronic Data Inter-change system of Customs. The details of the corresponding application shall be entered in the Electronic Data Inter-change system of Customs upon arrival of the goods in the Customs area. After goods are exported or order under section 51 of the Customs Act, 1962 (52 of 1962) has been issued, the rebate of excise duty shall, if the claim is found in order, be sanctioned and disbursed by the Assistant Commissioner of Customs or the Deputy Commissioner of Customs.

PROCEDURE FOR EXPORT TO ALL COUNTRIES (EXCEPT NEPAL AND BHUTAN) WITHOUT PAYMENT OF DUTY

The procedure for export of all excisable goods, except to Nepal and Bhutan, without payment of duty from the factory of the production or the manufacture or warehouse or any other premises as may be approved by the Commissioner of Central Excise, is governed by the provisions of Rule 19 of the Central Excise (No. 2) Rules, 2002. The conditions, limitations and safeguards are separately contained in Notification No. 42/ 2001-CE(NT) dated 26th June, 2002.

Conditions

(i) that the exporter shall furnish a General Bond (Surety/Security) to the Assistant Commissioner of Central Excise or the Deputy Commissioner of Central Excise having jurisdiction over the factory, warehouse or such approved premises, as the case may be, or the Maritime Commissioner or such other officer as authorised by the Board on this behalf, in a sum equal at least to the duty chargeable on the goods, with such surety or sufficient security, as such officers may approve for the due arrival thereof at the place of export and their export therefrom under Customs or as the case may be postal supervision. The manufacturer-exporter may furnish a letter of undertaking in the Form specified in lieu of a bond;

(ii) that goods shall be exported within six months from the date on which these were cleared for export from the factory of the production or the manufacture or warehouse or other approved premises within such extended period as the Assistant Commissioner of Central Excise or Deputy Commissioner of Central Excise or Maritime Commissioner may in any particular case allow;

(iii) that when the export is from a place other than registered factory or warehouse, the excisable goods are in original packed condition and identifiable as to their origin.

Procedure for removal without payment of duty

(a) After furnishing bond, a merchant-exporter shall obtain certificates in Form CT-1 issued by the Superintendent of Central Excise having jurisdiction over the factory or warehouse or approved premises or Maritime Commissioner or such other officer as may be authorised by the Board on this behalf and on the basis of such certificate he may procure excisable goods without payment of duty for export by indicating the quantity, value and duty involved therein;

(b) the exporter who has furnished bond shall ensure that the debit in bond account does not exceed the credit available therein at any point of time;

(c) the manufacturer-exporter may remove the goods without payment of duty after furnishing the letter of undertaking as specified under condition (1);

(d) such General bond or letter of undertaking shall not be discharged unless the goods are duly exported, to the satisfaction of the Assistant Commissioner of Central Excise or the Deputy Commissioner of Central Excise or Maritime Commissioner or such other officer as may be authorised by the Board on this behalf within the time allowed for such export or are otherwise accounted for to the satisfaction of such officer, or until the full duty due upon any deficiency of goods, not accounted so and interest, if any, has been paid.

Sealing of goods and examination at place of despatch

(a) For the sealing of goods intended for export at the place of despatch, the exporter shall present the goods along with four copies of application in the Form A.R.E.-I to the Superintendent or Inspector of Central Excise who will verify the identity of goods mentioned in the application and the particulars of the duty paid or payable, and if found in order, he shall seal each package or the container in the manner as may be specified by the Commissioner of Central Excise and endorse each copy of the application in token of having such examination done;

(b) the said Superintendent or Inspector of Central Excise shall return the original and duplicate copies of application to the exporter mid retain the quadruplicate copy;

(c) the triplicate copy of application shall be sent to the officer to whom bond or letter of undertaking has been furnished, either by post or by handing over to the exporter in a tamper proof sealed cover after posting the particulars in official records;

(d) the exporter may prepare quintuplicate copy of application for claiming any other export incentive. This copy shall be dealt in the same manner as the original copy of application;

(e) in case of export by parcel post after the goods intended for export has been sealed, the exporter shall affix to the duplicate application sufficient postage stamps to cover postal charges and shall present the documents, together with the package to which it refers, to the postmaster at the office of booking.

Despatch of goods by self-sealing and self-certification

(a) where the exporter desires self-sealing and self-certification for removal of goods from the factory, warehouse or any approved premises, the exporter or a person duly authorised, shall certify on all the copies of the application that the goods have been sealed in his presence, and shall send the original and duplicate copies of the application along with the goods at the place of export, and shall send the triplicate and quadruplicate copies of the application to the Superintendent or Inspector of Central Excise having jurisdiction over the factory, warehouse, any such approved premises within twenty four hours of removal of the goods;

(b) the Superintendent or Inspector of Central Excise shall, after verifying the particulars of the bond or letter of undertaking and endorsing the correctness or otherwise, of the particulars on the application, send to the officer to whom the bond or letter of undertaking has been furnished either by post or by handing over to the exporter in a tamper proof sealed cover after recording the particulars in the official records;

(c) The exporter may prepare quintriplicate copy of application for claiming any other export incentive. This copy shall be dealt in the same manner as the original copy of application;

Examination of goods at the place of export

(a) On arrival at the place of export, the goods shall be presented together with original, duplicate and quintuplicate (optional) copies of the application to the Commissioner of Customs or other duly appointed officer;

(b) The Commissioner of Customs or other duly appointed officer shall examine the goods with the particulars as specified in the application and if he finds that the same are correct arid exportable in accordance with the laws for the time being in force, shall allow export thereof and certify on the copies of the application that the goods have been duly exported citing the shipping bills.

CUSTOMS PROCEDURE FOR EXPORT

In India custom clearance is a complex and time taking procedure that every export face in his export business. Physical control is still the basis of custom clearance in India where each consignment is manually examined in order to impose various types of export duties. High import tariffs and multiplicity of exemptions and export promotion schemes also contribute in complicating the documentation and procedures. So, a proper knowledge of the custom rules and regulation becomes important for the exporter. For clearance of export goods, the exporter or export agent has to undertake the following formalities:

Registration

Any exporter who wants to export his good need to obtain PAN based Business Identification Number (BIN) from the Directorate General of Foreign Trade prior to filing of shipping bill for clearance of export goods. The exporters must also register themselves to the authorised foreign exchange dealer code and open a current account in the designated bank for credit of any drawback incentive.

Registration in the case of export under export promotion schemes

All the exporters intending to export under the export promotion scheme need to get their licences / DEEC book etc.

Processing of Shipping Bill - Non-EDI

In case of Non-EDI, the shipping bills or bills of export are required to be filled in the format as prescribed in the Shipping Bill and Bill of Export (Form) regulations, 1991. An exporter need to apply different forms of shipping bill/ bill of export for export of duty free goods, export of dutiable goods and export under drawback etc.

Processing of Shipping Bill - EDI

Under EDI System, declarations in prescribed format are to be filed through the Service Centers of Customs. A checklist is generated for verification of data by the exporter/CHA. After verification, the data is submitted to the System by the Service Center operator and the System generates a Shipping Bill Number, which is endorsed on the printed checklist and returned to the exporter/CHA. For export items which are subject to export cess, the TR-6 challans for cess is printed and given by the Service Center to the exporter/CHA immediately after submission of shipping bill. The cess can be paid on the strength of the challan at the designated bank. No copy of shipping bill is made available to exporter/CHA at this stage.

Quota Allocation

The quota allocation label is required to be pasted on the export invoice. The allocation number of AEPC (Apparel Export Promotion Council) is to be entered in the system at the time of shipping bill entry. The quota certification of export invoice needs to be submitted to Customs along-with other original documents at the time of examination of the export cargo. For determining the validity date of the quota, the relevant date needs to be the date on which the full consignment is presented to the Customs for examination and duly recorded in the Computer System.

Arrival of Goods at Docks

On the basis of examination and inspection goods are allowed enter into the Dock. At this stage the port authorities check the quantity of the goods with the documents.

System Appraisal of Shipping Bills

In most of the cases, a Shipping Bill is processed by the system on the basis of declarations made by the exporters without any human intervention. Sometimes the Shipping Bill is also processed on screen by the Customs Officer.

Customs Examination of Export Cargo

Customs Officer may verify the quantity of the goods actually received and enter into the system and thereafter mark the Electronic Shipping Bill and also hand over all original documents to the Dock Appraiser of the Dock who many assign a Customs Officer for the examination and intimate the officers' name and the packages to be examined, if any, on the check list and return it to the exporter or his agent. The Customs Officer may inspect/ examine the shipment along with the Dock Appraiser. The Customs Officer enters the examination report in the system. He then marks the Electronic Bill along with all original documents and check list to the Dock Appraiser. If the Dock Appraiser is satisfied that the particulars entered in the system conform to the description given in the original documents and as seen in the physical examination, he may proceed to allow "let export" for the shipment and inform the exporter or his agent.

Stuffing / Loading of Goods in Containers

The exporter or export agent hand over the exporter's copy of the shipping bill signed by the Appraiser "Let Export" to the steamer agent. The agent then approaches the proper officer for allowing the shipment. The Customs Preventive Officer supervising the loading of container and general cargo in to the vessel may give "Shipped on Board" approval on the exporter's copy of the shipping bill.

Drawal of Samples

Where the Appraiser Dock (export) orders for samples to be drawn and tested, the Customs Officer may proceed to draw two samples from the consignment and enter the particulars thereof along with details of the testing agency in the ICES/E system. There is no separate register for recording dates of samples drawn. Three copies of the test memo are prepared by the Customs Officer and are signed by the Customs Officer and Appraising Officer on behalf of Customs and the exporter or his agent. The disposal of the three copies of the test memo is as follows:-

- Original – to be sent along with the sample to the test agency.
- Duplicate – Customs copy to be retained with the 2nd sample.
- Triplicate – Exporter's copy.

The Assistant Commissioner/Deputy Commissioner if he considers necessary, may also order for sample to be drawn for purpose other than testing such as visual inspection and verification of description, market value inquiry, etc.

Amendments

Any correction/amendments in the check list generated after filing of declaration can be made at the service center, if the documents have not yet been submitted in the system and the shipping bill number has not been generated. In situations, where corrections are required to be made after the generation of the shipping bill number or after the goods have been brought into the Export Dock, amendments is carried out in the following manners.

1. The goods have not yet been allowed "let export" amendments may be permitted by the Assistant Commissioner (Exports).
2. Where the "Let Export" order has already been given, amendments may be permitted only by the Additional/Joint Commissioner, Custom House, in charge of export section.

In both the cases, after the permission for amendments has been granted, the Assistant Commissioner / Deputy Commissioner (Export) may approve the amendments on the system on behalf of the Additional /Joint Commissioner. Where the print out of the Shipping Bill has already been generated, the exporter may first surrender all copies of the shipping bill to the Dock Appraiser for cancellation before amendment is approved on the system.

Export of Goods under Claim for Drawback

After actual export of the goods, the Drawback claim is processed through EDI system by the officers of Drawback Branch on first come first served basis without feeling any separate form.

Generation of Shipping Bills

The Shipping Bill is generated by the system in two copies- one as Custom copy and one as exporter copy. Both the copies are then signed by the Custom officer and the Custom House Agent.

EXPORT RISK MANAGEMENT

Like any business transaction, risk is also associated with good to be exported in an overseas market. Export is risk in international trade is quite different from risks involve in domestic trade. So, it becomes important to all the risks related to export in international trade with an extra measure and with a proper risk management.

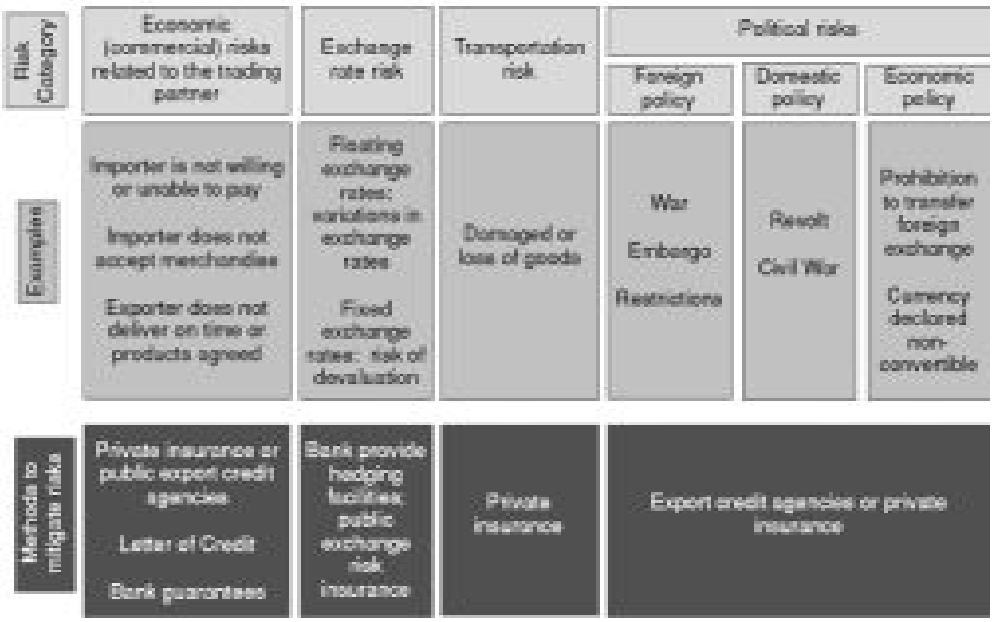
Types of risks

The various types of export risks involve in an international trade are as follow:

- ***Credit Risk:*** Sometimes because of large distance, it becomes difficult for an exporter to verify the creditworthiness and reputation of an importer or buyer. Any false buyer can increase the risk of non-payment, late payment or even straightforward fraud. So, it is necessary for an exporter to determine the creditworthiness of the foreign buyer. An exporter can seek the help of commercial firms that can provide assistance in credit-checking of foreign companies.
- ***Poor Quality Risk:*** Exported goods can be rejected by an importer on the basis of poor quality. So it is always recommended to properly check the goods to be exported. Sometimes buyer or importer raises the quality issue just to put pressure on an exporter in order to try and negotiate a lower price. So, it is better to allow an inspection procedure by an independent inspection company before shipment. Such an inspection protects both the importer and the exporter. Inspection is normally done at the request of importer and the costs for the inspection are borne by the importer or it may be negotiated that they be included in the contract price. Alternatively, it may be a good idea to ship one or two samples of the goods being produced to the importer by an international courier company. The final product produced to the same standards is always difficult to reduce.
- ***Transportation Risks:*** With the movement of goods from one continent to another, or even within the same continent, goods face many hazards. There is the risk of theft, damage and possibly the goods not even arriving at all.
- ***Logistic Risk:*** The exporter must understand all aspects of international logistics, in particular the contract of carriage. This contract is drawn up between a shipper and a carrier (transport operator). For this an exporter may refer to Incoterms 2000, ICC publication.
- ***Legal Risks:*** International laws and regulations change frequently. Therefore, it is important for an exporter to drafts a contract in conjunction with a legal firm, thereby ensuring that the exporter's interests are taken care of.
- ***Political Risk:*** Political risk arises due to the changes in the government policies or instability in the government sector. So it is important for an exporter to be constantly aware of the policies of foreign governments so that they can change their marketing tactics accordingly and take the necessary steps to prevent loss of business and investment.
- ***Unforeseen Risks:*** Unforeseen risk such as terrorist attack or a natural disaster like an earthquake may cause damage to exported products. It is therefore important that an exporter ensures a force majeure clause in the export contract.
- ***Exchange Rate Risks:*** Exchange rate risk is occurs due to the uncertainty in the future value of a currency. Exchange risk can be avoided by adopting Hedging scheme.

Methods and instruments to manage risks

The figure below shows some examples of the various types of risks and the methods that may be used to mitigate or reduce them.



Source: WTO, "Trade, Finance & Financial Crises", special studies 3

Some of the common financial instruments that importers and exporters can use to manage their risks are introduced below:

Forfaiting

Forfaiting is a term generally used to define the purchase or sale of rights and obligations arising from the delivery and acceptance of goods and services due at some future date and without recourse to any previous holder of the obligations. It is a form of supplier credit, which means that the supplier offers credit terms to the buyer and then sells the debt to a bank without recourse. This allows the seller to reduce his exchange rate risk and to eliminate most non-payment risks.

Hedging

Exporters and importers can manage foreign exchange risk by hedging. Hedging a particular currency exposure means offsetting a currency position by another so that whatever is lost or gained on the original currency exposure is offset by a corresponding foreign exchange gain or loss on the currency hedge. Hedging can reduce the volatility of a company's cash flows because the company's payments and receipts are not forced to fluctuate in accordance with currency movements. The two most common hedging methods are forward and future contracts.

(i) Forward contracts

A forward contract is a contract made today for delivery of an asset at a specified time in the future and at a price or exchange rate agreed upon today. The price is therefore fixed and will not be affected by currency fluctuation. Alternatively, a company can arrange a forward contract with its bank. This involves entering into a contract with a bank today under which the bank undertakes to exchange the foreign currency received from the company at an agreed exchanged rate. The agreed exchanged rate is usually the forward rate of the bank for a predetermined time frame (for example, six months).

(ii) Futures contracts

A futures contract is similar to a forward contract, but it is traded on organized exchanges with standardized terms (in contrast, forward contracts are traded over-the counter and are customized one-off transactions between a buyer and a seller). Intermediate gains or losses on a futures contract are posted each day during the life of the contract. Governments in emerging economies are also creating commodity futures exchanges to help producers and traders to manage their price risk and facilitate the price discovery process.

Export credit insurance

Export credit insurance (ECI) protects an exporter of products and services against the risk of non-payment by a foreign buyer. In other words, ECI significantly reduces the payment risks associated with doing international business by giving the exporter conditional assurance that payment will be made if the foreign buyer is unable to pay. Simply put, exporters can protect their foreign receivables against a variety of risks that could result in non-payment by foreign buyers. ECI generally covers commercial risks, such as insolvency of the buyer, bankruptcy, or protracted defaults (slow payment), and certain political risks such as war, terrorism, riots, and revolution. ECI also covers currency inconvertibility, expropriation, and changes in import or export regulations.ECI is offered either on a single-buyer basis or on a portfolio multi-buyer basis for short-term (up to one year) and medium-term (one to five years) repayment periods.

- ECI allows exporters to offer competitive open account terms to foreign buyers while minimizing the risk of non-payment.
- Even creditworthy buyers could default on payment due to circumstances beyond their control.
- With reduced non-payment risk, exporters can increase export sales, establish market share in emerging and developing countries, and compete more vigorously in the global market.
- When foreign accounts receivables are insured, lenders are more willing to increase the exporter's borrowing capacity and to offer attractive financing terms.

Pros

- Reduces the risk of non-payment by foreign buyers
- Offer open account terms safely in the global market

Cons

- Cost of obtaining and maintaining an insurance policy
- Risk sharing in the form of a deductible (coverage is usually below 100 percent)

An exporter may protect himself by purchasing ECI against non-payment for his trade receivables arising from either commercial or non-commercial risks. Depending on the type of ECI they select, exporters may protect themselves from risks associated with the non-acceptance of goods by the buyer, the failure of the buyer to pay the debt, the failure of foreign banks to honor documentary credits, as well as risks associated with war, riots and civil commotion, bans on foreign exchange transfers and currency devaluation. However, ECI does not usually cover risks normally covered by marine, fire and other types of insurance offered by traditional commercial insurance companies. ECI may be offered by both private insurance companies and government-backed export credit agencies.

In India Export Credit guarantee Corporation of India Limited offers different policies tailored to the specific needs of the exporter against various risks which include:

1. Standard Policy
2. Export Turnover Policy
3. Specific Shipments Policy
4. Exports (specific buyer) Policy
5. Buyer Exposure Policy
6. Consignment Exports Policy
7. Software Projects/ IT-enabled Services Policy
8. Small Exporters Policy

Details of ECGC policies are available on its website www.ecgc.in Payments for exports are open to risks even

at the best of times. The risks have assumed large proportions today due to the far-reaching political and economic changes that are sweeping the world. An outbreak of war or civil war may block or delay payment for goods exported. A coup or an insurrection may also bring about the same result. Economic difficulties or balance of payment problems may lead a country to impose restrictions on either import of certain goods or on transfer of payments for goods imported. In addition, the exporters have to face commercial risks of insolvency or protracted default of buyers. The commercial risks of a foreign buyer going bankrupt or losing his capacity to pay are aggravated due to the political and economic uncertainties. Thus, Export credit insurance is designed to protect exporters from the consequences of the payment risks, both political and commercial, and to enable them to expand their overseas business without fear of loss.

Exim Bank in India issues following guarantees directly or in participation with other banks, for project export contract.

Bid Bond: Bid Bond is generally issued for a period of six months.

Advance Payment Guarantee: Exporters are expected to secure a mobilisation advance of 10-20% of the contract value which is normally released against bank guarantee and is generally recovered on a pro-rata basis from the progress payments during project execution.

Performance Guarantee: Performance guarantee for 5-10% of contract is issued, valid upto completion of maintenance period normally one year after completion of contract period and/or grant of Final Acceptance Certificate (FAC) by the overseas employer. Format of guarantee is expected to be furnished by exporter, at least four weeks before actual issue, to facilitate discussions and formal approval.

Guarantee for Release of Retention Money: This enables the exporter to obtain the release of retention money (normally 10% of contract value) before obtaining Final Acceptance Certificate (FAC) from client.

Guarantee for Raising Borrowings Overseas: Bridge finance may be needed at the earlier phases of the contracts to supplement the mobilisation advance. Bridge finance upto 25% of the contract value may be raised in foreign currency from an overseas bank against this guarantee issued by a bank in India. Request for overseas borrowings must be supported by currency-wise cash flows, also indicating the outstanding letters of credit and L/C drawal schedule.

Other Guarantees: e.g. in lieu of customs duty or security deposit for expatriate labour.

Guarantee commission is charged at rates stipulated by the Foreign Exchange Dealers Association of India (FEDAI) or as stipulated by guarantee issuing bank. Margin requirement for issue of guarantee is generally waived by banks for Export Performance Guarantee. However, appropriate securities are availed of.

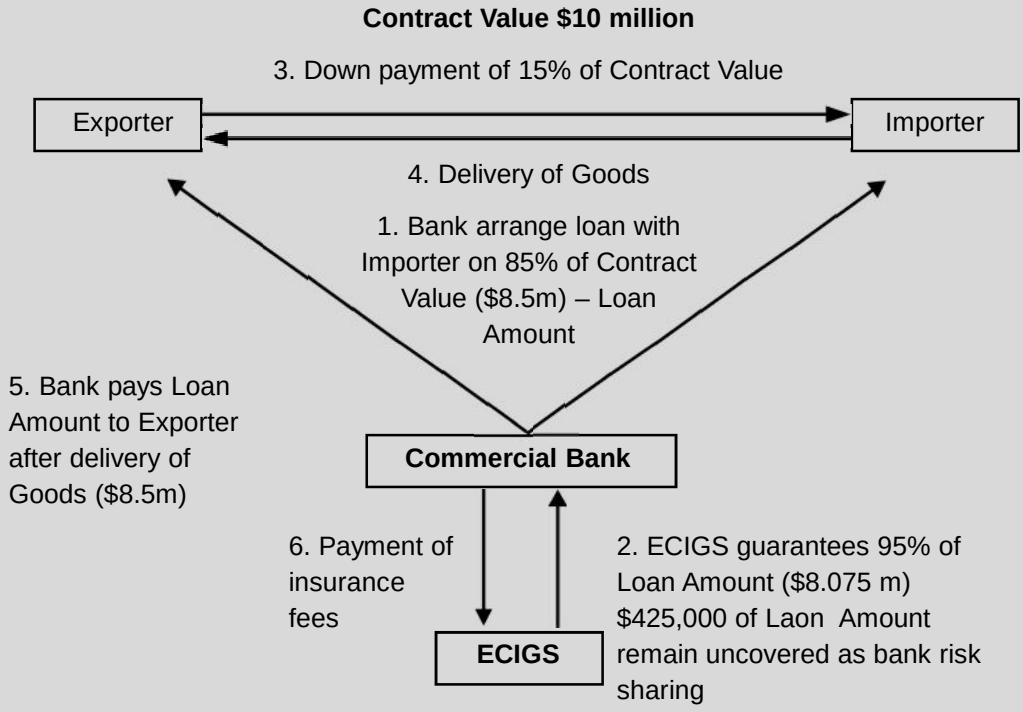
Export credit guarantee

Export credit guarantees are instruments to safeguard export-financing banks from losses that may occur from providing funds to exporters. While export credit insurance protects exporters, guarantees protect the banks offering the loans. They do not involve the actual provision of funds, but the exporters' access to financing is facilitated. An export credit guarantee is typically provided by a public institution or government agency to a commercial bank. Such a guarantee will allow exporters to secure pre-shipment financing or post-shipment financing from a bank more easily. Even in situations where trade financing is commercially available, banks may look unfavourably upon companies without sufficient track records. Therefore, providing the banking system with financial guarantees for purveying export credit is an important element in helping local companies to export. The agency providing this service has to carefully assess the risk associated with supporting the exporter as well as the buyer.

It is offered generally by a country's export promotion agency. It provides the insurance cover on an ad valorem fee that takes creditworthiness of the importer and country risk into consideration. Some agencies, such as export import banks, also offer discounting of the exporter's invoices. In India Export Credit guarantee Corporation of India Limited and EXIM offers guarantees to banks and financial institutions to enable exporters to obtain better facilities from them.

Export transaction with credit guarantee: An example

In this example, the exporter has successfully negotiated a contract worth US$ 10 million with an overseas buyer. However, the buyer has requested a 180-day credit. The exporter is not able to cope with the lack of cash flow or the risks of extending credit for the contract. His bank is also not willing to lend such a large amount without a guarantee.



The bank agrees, however, to arrange for a loan with the importer for 85 per cent of the total contract value (step 1). It the Export Credit Insurance and Guarantee Service (ECIGS, generally backed by the Government) provides a guarantee for 95 per cent of the loan value (step 2). This guarantee ensures that the bank will receive 95 per cent of the Loan value in case the buyer does not repay the loan.

Once the loan and guarantee are in place, the importer pays the exporter 15 per cent of the contract value (step 3). After delivery of the goods (step 4), the exporter claims the outstanding 85 per cent of the contract value from the bank. The bank remits the remaining 85 per cent of the contract value to the exporter after deducting the fee payable to EGIGS (step 6).

LESSON ROUND UP

- International Trade, "exports" refers to selling goods and services produced in the home country to other markets. In very simple terms, export may be defined as the selling of goods to a foreign country. There are many good reasons for exporting. Some of the motives of export are given below:
- The first and the primary reason for export is to earn foreign exchange. The foreign exchange not only brings profit for the exporter but also improves the economic condition of the country.
- The organisation should plan well before exporting as to what product to be exported, where to be exported etc. Once all the research and analysis is done by the exporting organisation, its time to get registered with the various government authorities before it starts to export.

- IEC Code is unique 10 digit code issued by DGFT – Director General of Foreign Trade, Ministry of Commerce, and Government of India to Indian Companies.
- An export license is a document issued by the appropriate licensing agency after which an exporter is allowed to transport his product in a foreign market.
- Export pricing is the most important factor in for promoting export and facing international trade competition.
- The Incoterms rules are an internationally recognized standard and are used worldwide in international and domestic contracts for the sale of goods.
- Pre-shipment documents are those that an exporter has to generate, authenticate and submit to the concerned authorities and departments to get the necessary clearances, prior to the actual shipment of the cargo, so that the cargo can be shipped out with valid documents.
- The post-shipment documents comprise the certified copies of some of the main pre-shipment documents and certain additional documents to be generated and compiled by the exporter so that the proof of shipments can be properly presented to the negotiating bank for collecting the payments through L/C or for presentation to the foreign buyer for collection of payment through the nominated bank.
- Letter of Credit also known as Documentary Credit is a written undertaking by the importers bank known as the issuing bank on behalf of its customer, the importer (applicant), promising to effect payment in favour of the exporter (beneficiary) up to a stated sum of money, within a prescribed time limit and against stipulated documents.
- Pre Shipment Finance is issued by a financial institution when the seller wants the payment of the goods before shipment. Post Shipment Finance is a kind of loan provided by a financial institution to an exporter or seller against a shipment that has already been made.
- In international trade, forfaiting may be defined as the purchasing of an exporter's receivables at a discount price by paying cash. By buying these receivables, the forfeiter frees the exporter from credit and the risk of not receiving the payment from the importer.
- Factoring is very simple and can be defined as the conversion of credit sales into cash. Here, a financial institution which is usually a bank buys the accounts receivable of a company usually a client and then pays up to 80% of the amount immediately on agreement.
- An important aspect about the goods to be exported is compulsory quality control and pre-shipment inspection. For this purpose, Export Inspection Council (EIC) was set up by the Government of India
- The primary role of packaging is to contain, protect and preserve a product as well as aid in its handling and final presentation.
- Packaging also refers to the process of design, evaluation, and production of packages. Risk management is a process of thinking analytically about all potential undesirable outcomes before they happen and setting up measures that will avoid them.
- A risk management plan helps an exporter to broaden the risk profile for foreign market.
- Foreign exchange risk in international trade arises from the fluctuation in price of one currency against another. This is a permanent risk that will remain as long as currencies remain the medium of exchange for commercial transactions.
- A bank guarantee is a written contract given by a bank on the behalf of a customer. By issuing this guarantee, a bank takes responsibility for payment of a sum of money in case, if it is not paid by the customer on whose behalf the guarantee has been issued.

- Export Credit Guarantee Corporation of India Limited, was established in the year 1957 by the Government of India to strengthen the export promotion drive by covering the risk of exporting on credit.
- Export-Import Bank of India is the premier export finance institution of the country, set up in 1982 under the Export-Import Bank of India Act 1981 with the objective for providing financial assistance to exporters and importers.

SELF TEST QUESTIONS

1. You are a company secretary of ABC exports Ltd. the company is newly formed and has just started its operations. You need to do planning for exports and advise the management. Explain how you will do planning for the exports.
2. Write a short note on Importer- Exporter Code Number.
3. Is registration of exporters compulsory? Explain the process of registering exporters with different authorities.
4. Explain the procedure of sending sample exports from India.
5. What are Incoterms? Explain the types and different Incoterms related to export pricing.
6. Write a note on Pre and post shipment documents.
7. What is letter of credit? Explain the types of letter of credit.
8. Describe different stages of pre-shipment finance.
9. Explain the types of post shipment finance.
10. Getting custom clearance is a tough task in India. Explain the process of getting custom clearance in India.
11. Write a brief note on central excise clearance formalities in India.
12. Write short note on following
    - Factoring
    - Quality control on Exports
    - EXIM Bank
    - ECGC

Lesson 6
International Trade and Regional Economic Integration

LESSON OUTLINE

- International Trade – Meaning
- Difference between International and Domestic Trade
- Reasons for International Trade
- Theories of International Trade
  - Mercantilism
  - Theory of absolute advantage by Adam Smith
  - Theory of comparative advantage by David Ricardo
  - Hecksher Ohlin Model
  - New trade theory: by Paul Krugman
- Recent trends in Global Trade
- Recent trends in India's foreign Trade
- Regional Economic Integration
- Regional Trading Blocs
- Types of Regional Trading Blocs
- Advantages of Regional Trading Blocs
- Disadvantages of Regional Trading Blocs
- Important Regional Trading Blocks of the World
    - ASEAN
    - EUROPEAN UNION
    - NAFTA
    - SAARC
    - SAPTA
    - SAFTA
- LESSON ROUND UP
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

If you walk into a supermarket and are able to buy American fruits, Brazilian coffee and a bottle of South African wine, you are experiencing the effects of international trade. International trade allows us to expand our markets for both goods and services. Today one can pick between a Japanese, German or American car. In the past few years global trade has grown leaps and bounds. Exports and imports form a reasonable part of every country's economy.

Industrialization, advanced transportation, globalization, multinational corporations, and outsourcing are all having a major impact on the international trade system. Moreover to promote international trade in the past decade, there has been an increase in trading blocs with more than one hundred agreements in place and more in discussion. Global trade has become the lifeline of every economy.

So in this chapter we try to explain international trade, why it started, theories of international trade, motivations and drivers of trade, nature of economic integration between nations and the stages in integration, explain the impact of economic integration among countries and various economic integrations across the globe.

"Coming together is a beginning; keeping together is progress; working together is success."

Henry Ford

INTERNATIONAL TRADE – MEANING

The world has a long, rich history of international trade among nations that can be traced back to early civilizations which had recognized that international trade can be tied directly to an improved quality of life for the citizens of all the partners. From the ancient Greeks to the present, government officials, intellectuals, and economists have pondered the determinants of trade between countries, have analyzed whether trade benefits or harms the nations, and, more importantly, have tried to determine what trade policy is best for any particular country. However, the development of international economics as an independent branch of economic theory is a relatively recent phenomenon. Today, the practice of trade among nations has grown by leaps and bounds. The economic, social, and political importance of international trade has increased manifold in recent centuries.

International trade is the exchange of capital, goods, and services across international borders or territories. In most countries, such trade represents a significant share of gross domestic product (GDP). Industrialization, advanced transportation, globalization, multinational corporations, and outsourcing are all having a major impact on the international trade system. International trade is also a branch of economics, which, together with international finance, forms the larger branch of international economics. Increasing international trade is crucial to the continuance of globalization. Without international trade, nations would be limited to the goods and services produced within their own borders.

DIFFERENCE BETWEEN INTERNATIONAL AND DOMESTIC TRADE

International trade is, in principle, not different from domestic trade as the motivation and the behavior of parties involved in a trade do not change fundamentally regardless of whether trade is across a border or not. The main difference is that international trade is typically more costly than domestic trade. The reason is that a border typically imposes additional costs such as tariffs, time costs due to border delays and costs associated with country differences such as language, the legal system or culture.

Another difference between domestic and international trade is that factors of production such as capital and labor are typically more mobile within a country than across countries. Thus international trade is mostly restricted to trade in goods and services, and only to a lesser extent to trade in capital, labor or other factors of production. Trade in goods and services can serve as a substitute for trade in factors of production. Instead of importing a factor of production, a country can import goods that make intensive use of that factor of production and thus embody it. An example is the import of labor-intensive goods by the United States from China. Instead of importing Chinese labor, the United States imports goods that were produced with Chinese labor.

REASONS FOR INTERNATIONAL TRADE

There are numerous reasons that encourage countries to engage in international trade. Some countries are deficient in critical raw materials, such as lumber or oil. To make up for these various deficiencies, countries must engage in international trade to obtain the resources necessary to produce the goods and/or services desired by their citizens. In addition to trading for raw materials, nations also exchange a wide variety of processed foods and finished products. Each country has its own specialties that are based on its economy and the skills of its citizens. The reasons or motivations for international trade depend a lot on the availability of the factors of production in the country. These factors can be commonly classified into capital, labor, and land.

Capital-intensive products, such as cars and trucks, heavy construction equipment, and industrial machinery, are produced by nations that have a highly developed industrial base. Japan is an example of a highly developed industrial nation that produces large quantities of high-quality cars for export around the world. Another reason Japan has adapted to producing capital-intensive products is that it is an island nation; there is little land available for land-intensive product production.

Labor-intensive commodities, such as clothing, shoes, or other consumer goods, are produced in countries that have relatively low labor costs and relatively modern production facilities. China, Indonesia, and the Philippines are examples of countries that produce many labor-intensive products.

Products that require large tracts of land, such as cattle production and wheat farming, are examples of land-intensive commodities. Countries that do not have large tracts of land normally purchase land-intensive products from countries that do have vast amounts of suitable land. The United States, for example, is one of the leading exporters of wheat. The combination of advanced farming technology, skilled farmers, and large tracts of suitable farmland in the Midwest and the Great Plains makes the mass production of wheat possible.

Over time a nation's work force will change, and thus the goods and services that nation produces and exports will change. Nations that train their workers for future roles can minimize the difficulty of making a transition to a new, dominant market. The United States, for example, was the dominant world manufacturer from the end of World War II until the early 1970s. But, beginning in the 1970s, other countries started to produce finished products more cheaply and efficiently than the United States, causing U.S. manufacturing output and exports to drop significantly. However, rapid growth in computer technology began to provide a major export for the United States. Practically speaking, the United States has been slowly transformed from a manufacturing-based economy into a new Information Age-based economy that relies on exporting cutting-edge technology as high tech software and computer companies proliferate.

Today hardly is there any country which is not engaged in International Trade. The economies of certain small countries are dependent mainly on International Trade. There are a number of factors which contribute to the development of foreign trade. Most important among them are:

1. **Natural Resources and Geographical Factors:** Each country differs in natural resources and geographical distribution of various factors of production. Diversities in natural and geographical distribution of various factors of production. Diversities in natural and geographical conditions make a country more efficient in the production of one commodity and another country in some other commodity. These countries specialise themselves in the production of such commodities and supply them to other countries in exchange for the commodities which they do not produce but other countries have specialisation in their production. For example, because of favourable natural conditions, India and Sri Lanka taken together produce 87% of the world total production of tea. Mica in India, manganese in Russia and oil in Arab countries are a few examples of this kind of specialisation.

2. **Occupation Distribution:** The population and its occupational distribution also differs from country to country. Occupational structure of its population decides the field of specialisation. For example, a large part of India's population is engaged in agriculture, hence it has specialised in the production of food grains and other agricultural products. England, on the other hand, has specialised itself in the production of Industrial goods as it has abundance of capital and scarcity of land and a large part of its population is engaged in Industries. Thus, countries specialise themselves on the basis of their occupations. Specialisation gives birth to international trade.

3. **Means of Transport:** Means and costs of transportation also contribute to the International trade. Industries using weight losing raw materials one generally localised at places near to the raw materials because the transport costs is the deciding factor. The countries where such raw materials are found in abundance, get specialised in their end-product. For example, India is a large producer of sugarcane and therefore, sugar industry is located mainly in India. At International level, the factors of production are not freely movable, because they involve high cost of transportation. Other countries, therefore cannot set up sugar industries and shall make imports of sugar from India and other sugar producing countries.

4. **Large-scale Production:** Large scale production of a commodity gives many advantages of scale. The industry of such a commodity can produce it at a lower cost because of scale economics and

specialisation. After meeting the demand for the commodity in the national market, the surplus can easily be exported at a price fetching and handsome profits to the industry. For example, an industrial unit producing locomotive engines for the Indian Railways, can specialise itself in the production of locomotives. Large scale production of locomotives may enable the unit to export them to neighbouring countries.

5. **Differences in Costs:** Production costs of a commodity differ from country to country due to a number of factors like Availability of natural resources and geographical conditions, Occupational structure, Large-scale production, Development in the field of science and technology etc. Countries having favourable conditions can produce the commodities at a lower costs and other countries at higher costs. Higher domestic costs of production shall encourage the imports of that commodity into the country and lower costs items may be exported.
6. **Degree of Self-sufficiency:** No country of the world is self-sufficient. The degree of self-sufficiency, however differs from country to country. For example the Russia imports 2% to 3% of its requirements and the USA only 4% to 5% of its total consumption. The degree of selfsufficiency is 40% to 50% in underdeveloped countries. Therefore, the countries which cannot produce at all or can produce only at a very high cost, arrange the supply of such goods through imports from other countries.

THEORIES OF INTERNATIONAL TRADE

The theory of trade has to answer one basic question as to “what determines trade” or “why do countries gain by trading”. The theories of trade are discussed below:

MERCANTILISM

The first reasonably systematic body of thought devoted to international trade is called “mercantilism” and it emerged in seventeenth and eighteenth century in Europe. An outpouring of pamphlets on economic issues, particularly in England and especially related to trade, began during this time. The doctrine of mercantilism had many modern features like it was very nationalistic and favored its own nation to be of prime importance. It generally viewed foreign trade with a suspicion.

The mercantilist writers argued that a key objective of trade should be to promote a favorable balance of trade. A “favorable” balance of trade is one in which the value of domestic goods exported exceeds the value of foreign goods imported. Trade with a given country or region was judged profitable by the extent to which the value of exports exceeded the value of imports, thereby resulting in a balance of trade surplus and adding precious metals and treasure to the country’s stock. Scholars later disputed the degree to which mercantilists confused the accumulation of precious metals with increase in national wealth. But without a doubt, mercantilists tended to view exports favorably and imports unfavorably.

Even if the balance of trade was not a specific source of concern, the commodity composition of trade was. Exports of manufactured goods were considered beneficial, and exports of raw materials were considered harmful; imports of raw materials were viewed as advantageous and imports of manufactured goods were viewed as damaging. This ranking of activities was based not only on employment grounds, where processing and adding value to raw materials was thought to generate better employment opportunities than just extraction or primary production of basic goods, but also for building up industries to strengthen the economy and the national defense.

Mercantilists advocated that government policy be directed to arrange the flow of commerce to conform these beliefs. They sought a highly interventionist agenda, using taxes on trade to manipulate the balance of trade or commodity composition of trade in favor of the home country. But even if the logic of mercantilism was correct, this strategy could never work if all nations tried to follow it simultaneously. This is due to the fact that not every country can have a balance of trade surplus, and not every country can export manufactured goods and import raw materials.

THEORY OF ABSOLUTE ADVANTAGE BY ADAM SMITH

The anti-mercantilist economic writers rebelled against the classical economists during the eighteenth century and advocated complete free trade and set out systematic reasons for believing that free trade might be desirable. Adam Smith was the first economists to support international trade in his book "**An Inquiry into the Nature and Causes of the Wealth of Nations**", published in 1776. Smith argued that economic growth depended upon specialization and the division of labour. Specialization helped promote greater productivity – that is, producing more goods from the same resources, which is essential for achieving higher standards of living. According to Smith, the division of labour was limited by the extent of the market; in other words, small markets would not be able to support a great deal of specialization, whereas larger markets could.

Adam Smith saw clearly that a country could gain by trading. As the tailor does not make his own shoes; he exchanges a suit for shoes. Thereby both the shoemaker and the tailor gain. In the same manner, Smith argued that the whole country can gain by trading with other countries.

If it takes 10 labor units to manufacture 1 unit of good A in country I but 20 labor units in country II, and if it takes 20 units of labor to manufacture 1 unit of good B in country I but only 10 labor units in Country II, then both countries can gain by trading.

If the two countries exchanged the 2 goods at a ratio of 1 to 1, so that 1 unit of good A is exchanged for 1 unit of good B, country I would get 1 unit of good B by sacrificing only 10 units of labor, whereas it would have to give up 20 units of labor if it produced the good itself. Likewise, country II would have to sacrifice only 10 units of labor to get 1 unit of good A, whereas it would have to sacrifice only 10 units of labor if it produced it itself. The implication of this is clearly that both countries could have more of both goods, with a given effort, by trading.

This was a simple and powerful illustration of the benefits of trade given by Adam Smith. The only assumption in this theory was non-interference for free trade as the best policy for trade between nations.

Thus it was opined that international trade effectively increased the size of the market for any given country, allowed for more refined specialization, created an international division of labour, and thereby benefited all countries by increasing the world's productivity and output.

Smith made a powerful case that government promotion of trade and government restriction of trade was unwise and harmful. He fundamentally changed the analysis of trade policy and essentially established the presumption that free trade was the best policy unless some other considerations overrode that presumption.

Adam Smith and the classical economists, claimed international trade was an efficient mechanism for allocating resources and for increasing national welfare, regardless of the level of a country's economic development. Any impediments to trade would detract from the gains from trade and therefore harm the economy. Smith and the classical economists made a powerful case for liberalizing trade from government restrictions (such as import tariffs and quotas) and moving towards free trade.

Smith's argument seems convincing, but it was not very deep. It was left to Torrens and Ricardo to produce the stronger and more subtle argument for the benefits of trade contained in the theory of comparative advantage.

THEORY OF COMPARATIVE ADVANTAGE BY DAVID RICARDO

The classical economists writing in the first quarter of the nineteenth century reinforced the case for free trade. The theory of comparative advantage emerged during this period and strengthened the understanding of the nature of trade and its benefits. David Ricardo has received most of the credit for developing this important theory, although James Mill and Robert Torrens had similar ideas around the same time.

The theory of comparative advantage suggests that a country should export goods in the country in which its relative cost advantage, and not the absolute cost advantage, is greatest in comparison to other countries.

According to Smith, if one country has an absolute advantage over the other country in one line of production and the other country has an absolute advantage over the first country in a second line of production; both countries can gain by trading. But what if one country is more productive than another country is in all lines of production? Ricardo claimed that if country I can produce all goods with less labor cost than country II then also it will benefit the countries to trade so long as long as country II is not equally less productive in all lines of production.

Ricardo used England and Portugal as examples in his demonstration, the two goods they produced being wine and cloth. Ricardo assumed that Portugal was more efficient in making both cloth and wine. Table 1.1 shows how Ricardo summed up the cost conditions in the two countries.

Table 1.1

Cost comparisons

Labour cost of production (in hours)

	1 unit of wine	**1 unit of cloth**
Portugal	80	90
England	120	100

According to this model, Portugal has an absolute advantage in the production of wine as well as in the production of cloth, because the labor cost of production for each unit of the two commodities is less in Portugal than in England.

To demonstrate that trade between England and Portugal will, even in this case, lead to gains for both countries, it is useful to introduce the concept of opportunity cost. The opportunity cost for a good X is the amount of other goods which have to be given up in order to produce one (additional) unit of X. Table 1.2 gives the opportunity costs for producing wine and cloth in Portugal and England. These costs have been constructed on the basis of the information given in Table 1.1.

Table 1.2

Opportunity costs

Opportunity costs for

	Wine	**Cloth**
Portugal	80/90 = 8/9	90/80 = 9/8
England	120/100 = 12/10	100/120 = 10/12

A country has a comparative advantage in producing a good if the opportunity cost for producing the good is lower at home than in the other country. Table 1.2 shows that Portugal has the lower opportunity cost of the two countries in producing wine, while England has the lower opportunity cost in producing cloth. Thus Portugal has a comparative advantage in the production of wine and England has a comparative advantage in the production of cloth.

We should now further clarify the meaning of the term ‘comparative advantage’. In order to speak about comparative advantage there must be at least two countries and two goods. We compare the opportunity costs of production of each good in both countries. As long as the two countries’ opportunity costs for one good differ, one country has a comparative advantage in the production of one of the two goods, while the other country has a comparative advantage to the production of the other good. As long as this is the case, both countries will gain from trade, regardless of the fact that one of the countries might have an absolute disadvantage in both lines of production.

The comparative advantage proposition states that a less developed country that lacks an absolute advantage in any goods can still engage in mutually beneficial trade, and that an advanced country whose domestic industries are more efficient than those in any other country can still benefit from trade even as some of its industries face intense import competition.

HECKSHER OHLIN MODEL

The Heckscher-Ohlin theory is usually formulated in terms of a two-factor model, with labor and capital as the two factors of production.

According to the Heckscher-Ohlin theory, what determines trade is differences in factor endowments. Some countries have much capital, others have much labor. The theory says that countries that are rich in capital will export capital-intensive goods, and countries that have much labor will export labor-intensive goods.

The following five assumptions are essential to the analysis : (1) there are no transport costs or other impediments to trade; (2) there is perfect competition in both commodity and factor markets; (3) all production functions are homogeneous of the first degree; (4) the production functions are such that the two commodities show different factor intensities; and (5) the production functions differ between commodities, but are the same in both countries, i.e., good A is produced with the same technique in both countries and good B is produced with the same technique in both countries.

NEW TRADE THEORY: BY PAUL KRUGMAN

Ricardo showed that every country (and every person) has a comparative advantage, a good or service that they can produce at a lower (opportunity) cost than any other country (or person). As a result, production is maximized when each country specializes in the good or service that they produce at lowest cost, that is in the good in which they have a comparative advantage. Since specialization in comparative advantage maximizes production, trade can make every country better off.

But what determines comparative advantage? In Ricardo it is the natural products of the soil, Portugal is good at producing wine and so England has a comparative advantage in cloth. Heckscher, Ohlin and Samuelson among others extended the model to show how factor proportions can determine comparative advantage - countries with a lot of labor relative to capital, for example, will tend to have a comparative advantage in labor intensive goods production.

However, that in the Ricardian model and its extensions the determinants of comparative advantage like geography and factor proportions lie outside of the model. New Trade Theory of which Paul Krugman can be said to be the founder, brings the determinants of comparative advantage into the model.

Consider the model in which there are two countries. In each country, consumers have a preference for variety but there is a tradeoff between variety and cost, consumers want variety but since there are economies of scale - a firm's unit costs fall as it produces more - more variety means higher prices. Preferences for variety push in the direction of more variety, economies of scale push in the direction of less. So suppose that without trade country I produces varieties A, B, C and country II produces varieties X, Y, Z. In every other respect the countries are identical so there are no traditional comparative advantage reasons for trade.

Nevertheless, if trade is possible it is welfare enhancing. With trade, the scale of production can increase which reduces costs and prices. The number of world varieties will decrease even as the number of varieties available to each consumer increases. That is, with trade, production will concentrate in say A, B, X, Y so each consumer has increased choice even as world variety declines.

Increasing variety for individuals even as world variety declines is a fundamental fact of globalization. In the context of culture, Tyler explains this very well in his book, 'Creative Destruction'; when people in Beijing can eat at McDonald's and people in America can eat at great Chinese restaurants the world looks increasingly similar even as each world resident experiences an increase in variety.

Thus, Krugman provided another reason why trade can be beneficial and a fundamental insight into globalization.

RECENT TRENDS IN GLOBAL TRADE

Four years after the onset of the global financial crisis, the world economy is struggling. There is weak global recovery across the board. The transfer of economic power from developed to emerging economies is speeding up. A large amount of political and economic turmoil has been witnessed over the past twelve months, from uprisings in the Middle East and North Africa to the tsunami in Japan and the sovereign debt crisis in the Euro Zone. Resulting volatility in commodity prices, disruptions to supply chains and general uncertainty has impacted businesses across the globe, slowing the recovery in both mature and emerging markets.

The crisis has produced a wide-ranging yet differentiated impact across the globe which inter-alia includes deceleration of growth, economic slowdown, contraction in world trade and reduced access to trade finance and negative effects on trade balances and balance of payments. Besides, this has resulted in dwindling levels of FDI, massive reversal of private capital flows, severe damage to the housing market, the banking sector and the financial sector as a whole, and, above all, reduced public confidence in financial institutions.

Global Economic Growth

The developments in the large industrial nations are not encouraging, leading to a downward revision in the global growth projections from 3.9% in 2011 to 3.2% in 2012 and 3.5% in 2013 as per the IMF World Economic Outlook (WEO), January, 2013. The outlook for growth in world trade has also been downgraded by WTO, from 3.7% in April, 2012, to 2.5% in September, 2012. All these factors have combined to impact Indian export prospects as well.

The IMF WEO, January, 2013, also mentions that global growth will strengthen gradually through 2013, averaging 3.5 percent on an annual basis, a moderate increase from 3.2 percent in 2012, but 0.1 percentage point lower than projected in the October 2012, WEO. A further strengthening to 4.1 percent is projected for 2014, assuming recovery takes a firm hold in the euro area economy.

Economic conditions improved modestly in the third quarter of 2012, with global growth increasing to about 3 percent. The main sources of acceleration were emerging market economies, where activity picked up broadly as expected, and the United States. Global financial conditions improved further in the fourth quarter of 2012. However, a broad set of indicators for global industrial production and trade suggests that global growth did not strengthen, further.

Turning to the updated outlook, growth in the United States is forecast to average 2 percent in 2013, rising above trend in the second half of the year. These forecasts are broadly unchanged from the October 2012 WEO, as underlying economic conditions remain on track. In particular, a supportive financial market environment and the turnaround in the housing market have helped to improve household balance sheets and should underpin firmer consumption growth in 2013.

The near-term outlook for the Euro Area has been revised downward, even though progress in national adjustment and a strengthened EU-wide policy response to the Euro Area crisis reduced risks and improved financial conditions for sovereigns in the periphery. Activity is now expected to contract by 0.2 percent in 2013.

Growth in emerging market and developing economies is on track to build to 5.5 percent in 2013. Nevertheless, growth is not projected to rebound to the high rates recorded in 2010–11. Supportive policies have underpinned much of the recent acceleration in activity in many economies. But, weakness in advanced economies will weigh on external demand, as well as, on the terms of trade of commodity exports, given the assumption of lower commodity prices in 2013.

Most advanced economies face two challenges. First, they need steady and sustained fiscal consolidation. Second, financial sector reform must continue to decrease risks in the financial system. Addressing these challenges will support recovery and reduce downside risks.

In China, ensuring sustained rapid growth requires continued progress with market-oriented structural reforms and rebalancing of the economy more toward private consumption. In other emerging market and developing economies, requirements differ.

World Trade: Shifting Pattern

In the decades following the end of colonial rule, the share of developing economies in world merchandise exports fell from 34 per cent in 1948 to 24 per cent in 1973, as exports of manufactures from the developed world rapidly increased. Thereafter, as many developing countries turned into increasingly important exporters of manufactured goods, their shares in aggregate merchandise exports recovered to 33 per cent in 2003 and further to 44 per cent by 2010.

In the sphere of merchandise imports, Asia (excluding Japan), Latin America, Africa and the Middle East together, the share of global merchandise imports increased from 28 to 38 per cent between 1993 and 2010. The share of the developed western economies and Japan dropped from 71 to 59 per cent in the same period. This process is likely to accelerate in the coming decades.

The other notable development in the international trade is the increasing regional concentration of merchandise trade. In 2010, the second largest regional trade was located in Asia (excluding Middle East) amounting in value to US $2.5 trillion or 62 per cent of the regional trade concentration after Europe which amounted to US $4.0 trillion. The proportion of Asian origin exports to other Asian markets has increased from 47 per cent in 1999 to 53 per cent in 2010. Not only is the developing world as a whole and Asia in particular becoming proportionately more important in international trade, but the trade within the region and potentially with Africa and Latin America hold the promise of further expansion and deepening. South-South trade has multiplied more than 10 times in the last two decades as compared to global trade which grew 4-fold in this period.

Table 2.1: World Economic Growth Estimates for 2012 and 2013

(Annual % Change)

	UN			IMF			World Bank		
	2012	**2013**	**2014**	**2012**	**2013**	**2014**	**2012**	**2013**	**2014**
World	2.2	2.4	3.2	3.2	3.5	4.1	2.3	2.4	3.1
Developed Countries	1.1	1.1	2	1.3	1.4	2.2	1.3	1.3	2
Euro Zone	-0.3	0.6	1.7	-0.4	-0.2	1	-0.4	-0.1	0.9
US	2.1	1.7	2.7	2.3	2	3	2.2	1.9	2.8
Japan	1.5	0.6	0.8	2	1.2	0.7	1.9	0.8	1.2
Developing Countries	4.7	5.1	5.6	5.1	5.5	5.9	5.1	5.5	5.7
LAC	3.1	3.9	4.4	3	3.6	3.9	3	3.5	3.9
Brazil	1.3	4	4.4	1	3.5	4	0.9	3.4	4.1
Russia	3.7	3.6	4.2	3.6	3.7	3.8	3.5	3.6	3.9
India	5.5	6.1	6.5	4.5	5.9	6.4	5.1	6.1	6.8
China	7.7	7.9	8	7.8	8.2	8.5	7.9	8.4	8

Source : UN, World Economic Situation and Prospects, 2013; IMF, World Economic Outlook, January 2013; World Bank, Global Economic Prospects, January 2013.

World Trade Scenario

As per IMF's World Economic Outlook January, 2013, the volume of world trade (goods and services) in 2012 slowed down to 2.8 per cent compared to the 5.9 per cent achieved in 2011. As per IMF projections, growth in the volume of world trade is expected to rise to 3.8 per cent in 2013.

The IMF has put its growth projections of world output at 3.5 per cent in 2013. The advanced economies are expected to grow at 1.4 per cent while the emerging and developing economies to grow at 5.5 per cent in 2013. The projected growth rates in different countries are expected to determine the markets for our exports.

As per WTO's International Trade Statistics, 2012, in merchandise trade, India is the 19th largest exporter in the world with a share of 1.7 per cent and the 12th largest importer with a share of 2.5 per cent in 2011.

Trade Slow Down

According to WTO Press Release dated 21st September, 2012, slowing global output growth has led World Trade Organization (WTO) to downgrade its 2012 forecast for world trade expansion to 2.5% in September, 2012 from 3.7% in April, 2012 and to scale back their 2013 estimate to 4.5% from 5.6% for the same period. On the export side, developed economies' trade is anticipated to grow at 1.5% increase in (down from 2%) and a 3.5% expansion for developing countries (down from 5.6%) is expected. On the import side, nearly stagnant growth of 0.4% in developed economies (down sharply from 1.9%) is forecast and a more robust 5.4% increase for developing countries (down from 6.2%) is expected.

In the Annual Report by the Director General on overview of developments in the international trading environment covering the period October 2011 to October 2012, the slowdown in trade in the first half of 2012 has been attributed to a marked deceleration in imports of developed countries and by a corresponding weakness in the exports of developing economies.

The WTO report has also pointed towards a slowdown in the imposition of new trade restrictive measures, though these continue to add to the existing trade restrictions and distortions put in place since the outbreak of the global crisis, most of which remain in effect and those that have existed for a long time. The persistence of the global economic crisis is fuelling the political and economic pressures put on governments to raise trade barriers. On the positive side the report shows that some countries have also adopted measures to streamline customs procedures.

RECENT TRENDS IN INDIA'S FOREIGN TRADE

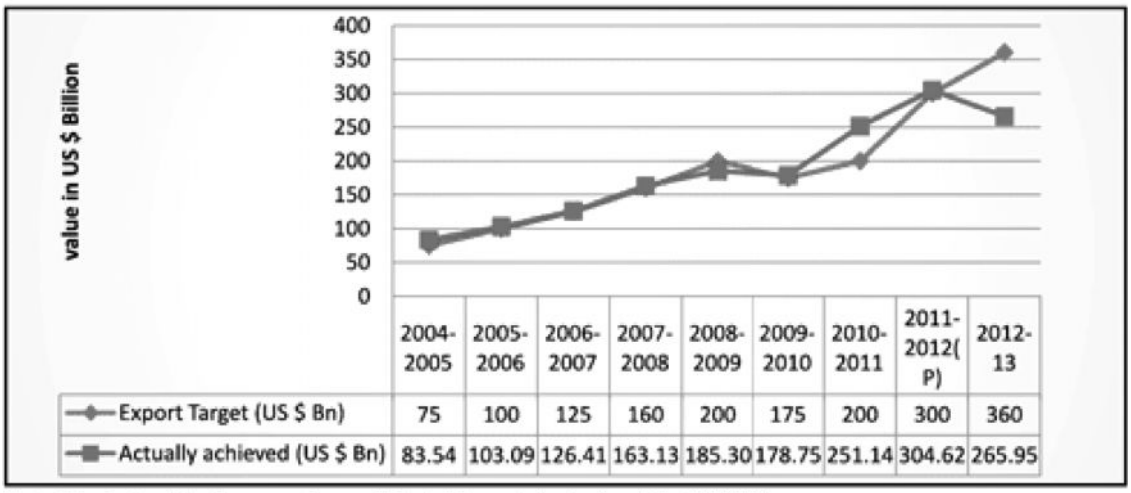
India's Trade Performance

India's merchandise exports reached a level of US $ 304.62 billion during 2011-12 registering a growth of 21.30 percent as compared to a growth of 40.49 percent during the previous year. Despite the recent setback faced by India's export sector due to global slowdown, merchandise exports still recorded a Compound Annual Growth Rate (CAGR) of 20.3 per cent from 2004-05 to 2011-12.

Exports

Exports recorded a growth of 21.30 per cent during Apr-Mar 2011-12. The Government has set an export target of US $ 360 billion for 2012-13. The merchandise exports have reached US $ 265.95 billion in 2012-13 (Apr.-Feb.). Export target and achievement from 2004-05 to 2011-12 and 2012-13 (Apr.-Feb.) is given in the Chart 3.1 below:

Chart 3.1
Export Target & Achievement



	2004-2005	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010	2010-2011	2011-2012(P)	2012-13
Export Target (US $ Bn)	75	100	125	160	200	175	200	300	360
Actually achieved (US $ Bn)	83.54	103.09	126.41	163.13	185.30	178.75	251.14	304.62	265.95

Note: The last cell in the second row of the table pertains to Apr.-Feb. 2012-13

Imports

Cumulative value of imports during 2012-13 (Apr.-Feb.) was US $ 448.04 billion as against US $ 446.94 billion during the corresponding period of the previous year registering a growth of 0.25 per cent in $ terms. Oil imports were valued at US $ 155.57 billion during 2012-13 (Apr.-Feb.) which was 11.92 per cent higher than oil imports valued US $ 139.00 billion in the corresponding period of previous year. Non-oil imports were valued at US $ 292.47 billion during 2012-13 (Apr.-Feb.) which was 5.03 per cent lower than non-oil imports of US $ 307.94 billion in previous year.

Trade Balance

The Trade deficit in 2012-13 (Apr.-Feb.) was estimated at US $ billion 182.09 which was higher than the deficit of US $ 169.81 billion during 2011-12 (Apr.-Feb.). Performance of Exports, Imports and Balance of Trade during 2004-05 to 2012-13 (April-Feb.) is given in the table below:

(Values in Rs crores)

S.No	Year	Exports	%Growth	Imports	%Growth	Trade Balance
1	2004-2005	3,75,340	27.94	5,01,065	39.53	-1,25,725
2	2005-2006	4,56,418	21.60	6,60,409	31.80	-2,03,991
3	2006-2007	5,71,779	25.28	8,40,506	27.27	-2,68,727
4	2007-2008	6,55,864	14.71	10,12,312	20.44	-3,56,448
5	2008-2009	8,40,755	28.19	13,74,436	35.77	-5,33,680
6	2009-2010	8,45,534	0.57	13,63,736	-0.78	-5,18,202
7	2010-2011	11,42,922	35.17	16,83,467	23.45	-5,40,545
8	2011-2012(Provisional)	14,59,281	27.68	23,44,772	39.28	-8,85,492
9	2011-12 (April-February) Press Release	13,20,836		21,32,198		-8,11,362

10	2012-13 (April-February) Press Release	14,46,627	9.52	24,36,564	14.27	-9,89,938

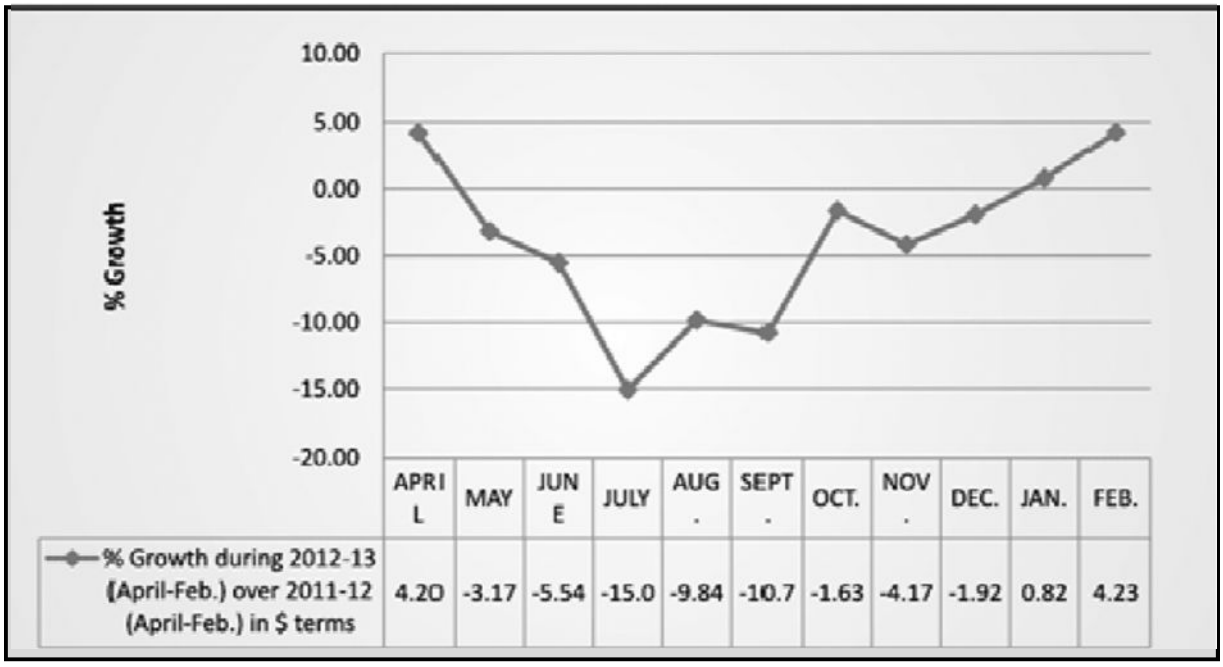
Data Source : DGCIS, Kolkata

(Values in US$ Millions)

S.No.	Year	Exports	%Growth	Imports	%Growth	Trade Balance
1	2004-2005	83,536	30.85	1,11,517	42.70	-27,981
2	2005-2006	1,03,091	23.41	1,49,166	33.76	-46,075
3	2006-2007	1,26,414	22.62	1,85,735	24.52	-59,321
4	2007-2008	1,63,132	29.05	2,51,654	35.49	-88,522
5	2008-2009	1,85,295	13.59	3,03,696	20.68	-1,18,401
6	2009-2010	1,78,751	-3.53	2,88,373	-5.05	-1,09,621
7	2010-2011	2,51,136	40.49	3,69,769	28.23	-1,18,633
8	2011-2012(Provisional)	3,04,624	21.30	4,89,181	32.29	-1,84,558
9	2011-12 (April-February) Press Release	2,77,125		4,46,939		-1,69,814
10	2012-13 (April-February) Press Release	2,65,946	-4.03	4,48,037	0.25	-1,82,090

Data Source: DGCIS, Kolkata

Chart 3.2
Month-wise Growth in Exports during 2012-13 (Apr.- Feb.) over 2011-12 (Apr.-Feb.)

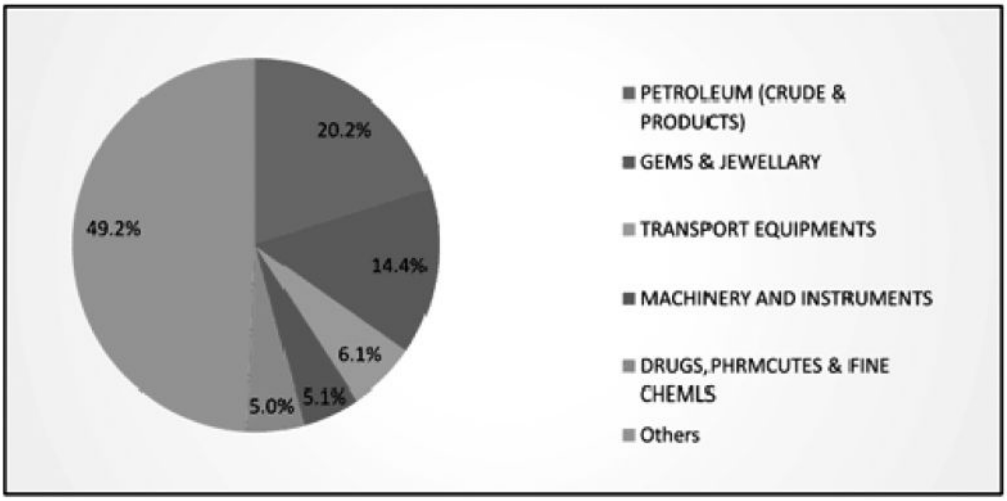


Exports of Principal Commodities

Exports of the top five commodities during the period 2012-13 (April-January) registered a share of 50.8 per cent in US $ terms mainly due to significant contribution in the exports of Petroleum (Crude & Products), Gems & Jewellery, Transport Equipments, Machinery and Instruments and Drugs, Pharmaceuticals & Fine Chemicals.

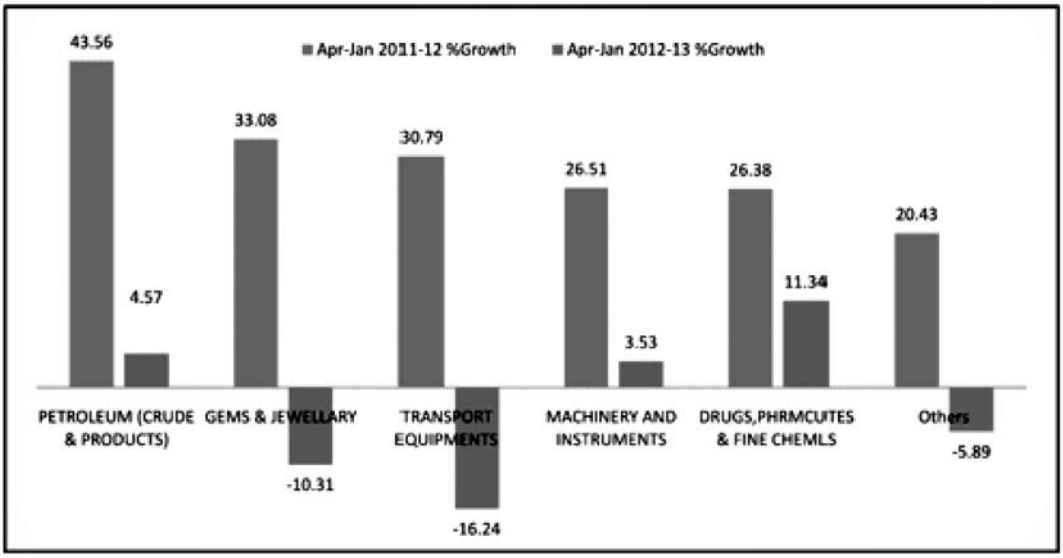
The share of top five Principal Commodity Groups in India's total exports during 2012-13 (April-January) is given at Chart 3.3.

Chart 3.3
Share of Top Five Commodities in India's Exports 2012-13
(April- January)



The export performance (in terms of growth in US $ terms) of top five commodities during 2012-13 (April-January) vis-a-vis the corresponding period of the previous year is shown in Chart 3.4.

Chart 3.4
Top Five Commodities of Exports by Growth (Apr. -Jan.) 2011-12 & 2012-13



Plantation Crops

Export of Plantation crops during 2012-13 (April–January), decreased by 9.95 per cent in US $ terms compared with the corresponding period of the previous year. Export of Coffee registered a negative growth of 11.44 per cent, the value decreasing from US $ 741.05 million to US $ 656.26 million. Export of Tea also decreased by 8.50 per cent.

Agriculture and Allied Products

Agriculture and Allied Products as a group include Cereals, Pulses, Tobacco, Spices, Nuts and Seeds, Oil Meals, Guargum Meals, Castor Oil, Shellac, Sugar & Molasses, Processed Food, Meat & Meat Products, etc. During 2012-13 (April–January), exports of commodities under this group registered a growth of 27.57 per cent with the value of exports increasing from US $ 21353.59 million in the previous year to US $ 27240.35 million during the current year.

Ores and Minerals

Exports of Ores and Minerals were estimated at US $ 4389.03 million during 2012-13 (April-January) registering a negative growth of 35.48 per cent over the same period of the previous year. Sub groups viz. Iron Ore, Mica, Other ores & minerals and Coal have recorded a negative growth of 64.99 per cent, 0.80 per cent, 9.46 per cent and 5.24 percent respectively. Processed minerals registered a growth of 12.14 per cent.

Leather and Leather Manufactures

Export of Leather and Leather Manufactures recorded a negative growth of 2.22 per cent during 2012-13 (April-January). The value of exports decreased to US $ 3973.92 million from US $ 4064.33 million during the same period of the previous year. Exports of Leather and Manufactures have registered a growth of 3.98 per cent and Leather Footwear registered a negative growth of 10.01 per cent.

Gems and Jewellery

The export of Gems and Jewellery during 2012-13(April-January) decreased to US $ 34758.78 million from US $ 38755.30 million during the corresponding period of last year showing a negative growth of 10.31 per cent.

Chemicals and Related Products

During the period 2012-13 (April-January), the value of exports of Chemicals and Related Products increased to US $ 34686.90 million from US $ 32319.14 million during the same period of the previous year registering a growth of 7.33 per cent. Basic Chemicals and Pharmaceuticals & Cosmetics and Rubber, Glass & Other Products have registered a positive growth and Residual Chemicals and allied products and Plastic & linoleum registered a negative growth.

Engineering Goods

Items under this group consist of Machinery, Iron & Steel and Other Engineering items. Export from this sector during the period 2012-13(April-January) stood at US $ 45543.37 million compared with US $ 47966.60 million during the same period of the previous year, registering a negative growth of 5.05 per cent. The growth in export of Other Engineering items stood at 5.78 per cent, Machinery & Instruments stood at 3.53 per cent and Machine Tools stood at 4.59 per cent.

Electronic Goods

During the period 2012-13 (April-January), exports of Electronic Goods as a group was estimated at US $ 7102.84 million compared with US $ 7441.50 million during the corresponding period of last year, registering a negative growth of 4.55 per cent.

Textiles

During the period 2012-13 (April-January), the value of Textiles exports was estimated at US $ 21200.12 million compared with US $ 22447.75 million in the corresponding period of the previous year, recording a negative growth of 5.56 per cent. The export of Readymade Garments, Manmade Textiles & Made Ups, Natural Silk Textiles, Wool and Woolen manufactures, Coir and coir manufactures and Jute manufactures registered negative growth of 7.80 per cent, 12.61 per cent, 23.34 per cent, 19.98 per cent, 7.18 per cent and 16.37 per cent respectively. However, Cotton yarn/Fabrics/Made-ups etc. registered a positive growth of 6.38 per cent.

Handicrafts and Carpets

Exports of Handicrafts declined to US $ 180.51 million during 2012-13 (April- January), from US $ 214.84 million during the corresponding period of the previous year registering a negative growth of 15.98 per cent. Export of carpets increased to US $ 812.17 million from US $ 699.26 million during the same period last year registering a growth of 16.15 per cent.

Project Goods

During 2012-13 (April-January), the export of Project Goods were estimated at US $ 87.70 million compared with US $ 44.10 million during the corresponding period of last year registering a substantial growth of 98.88 per cent.

Petroleum Products

Export of Petroleum Products increased to US $ 48613.38 million during 2012-13 (April- January), as compared with US $ 46489.12 million during the same period of last year recording a growth of 4.57 per cent.

Cotton Raw including Waste

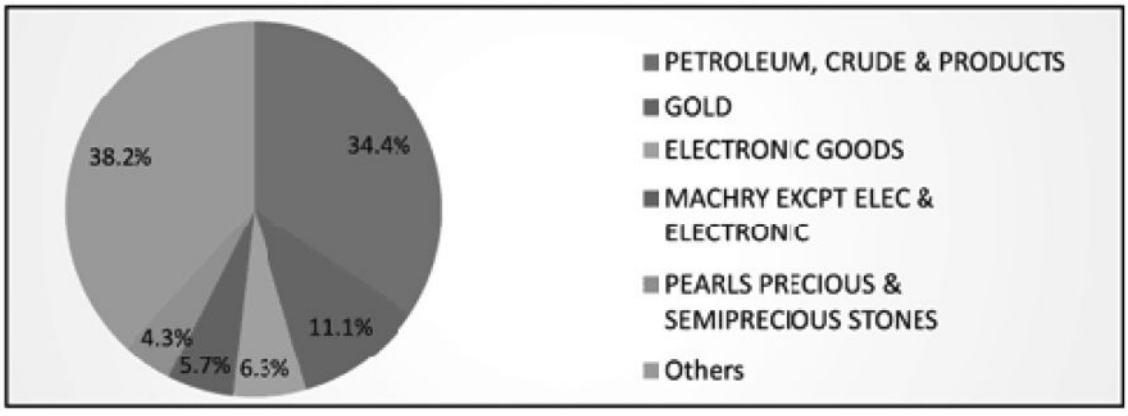
There was a negative growth in the exports of Cotton Raw including waste by 21.13 per cent from US $ 3326.67 million in 2011-12 (April-January) to US $ 2623.68 million during 2012-13 (April-January).

Imports of Principal Commodities

Imports of the top five commodities during the period 2012-13 (April-January) registered a share of 61.8 per cent mainly due to significant imports of Petroleum (Crude & Products), Gold, Electronic Goods, Machinery except electrical and electronic and Pearls, precious and semi-precious stones.

The share of top five Principal Commodity in India's total imports during 2012-13 (April– January) is given at Chart 3.5.

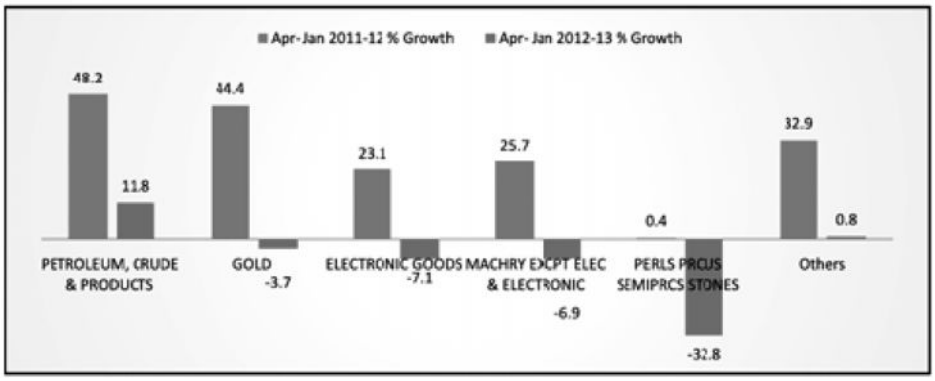
Chart 3.5
Share of Top Five Commodities in India's Imports 2012-13
(April- January)



The import performance by growth of top five Principal commodities during 2012-13 (April–January) vis-a-vis the corresponding period of the previous year is shown at Chart 3.6.

Chart 3.6

Top Five Commodities of Import by Growth (Apr. -Jan.) 2011-12 & 2012-13



Fertilizers

During 2012-13 (April– January), import of Fertilizers (manufactured) decreased to US $ 6991.61 million from US $ 8718.13 million in April-January 2011-12 recording a negative growth of 19.80 per cent.

Petroleum Crude & Products

The import of Petroleum Crude & Products stood at US $ 140729.62 million during 2012-13 April - January as against US $ 125871.43 million during the same period of the previous year registering a growth of 11.80 per cent.

Pearls, Precious and Semi-Precious Stones

Import of Pearls, Precious and Semi-Precious Stones during 2012-13 (April– January) decreased to US $ 17696.44 million from US $ 26339.27 million during the corresponding period of the previous year registering a substantial decline of 32.81 per cent.

Capital Goods

Import of Capital Goods, largely comprises of Machinery, including Transport Equipment and Electrical Machinery. Import of Machine Tools, Non-Electrical Machinery, and Electrical Machinery registered a negative growth of 4.67 per cent, 6.94 per cent, 6.45 per cent respectively and Transport Equipment registered a positive growth of 0.04 per cent.

Organic and Inorganic Chemicals

During 2012-13 (April–January), import of Organic and Inorganic Chemicals increased to US $ 16116.77 million from US $ 15837.29 million during the same period of last year, registering a growth of 1.76 per cent. Import of Medicinal and Pharmaceutical Products increased to US $ 2550.01 million from US $ 2446.88 million during the corresponding period of last year registering a growth of 4.21 per cent

Coal, Coke & Briquettes

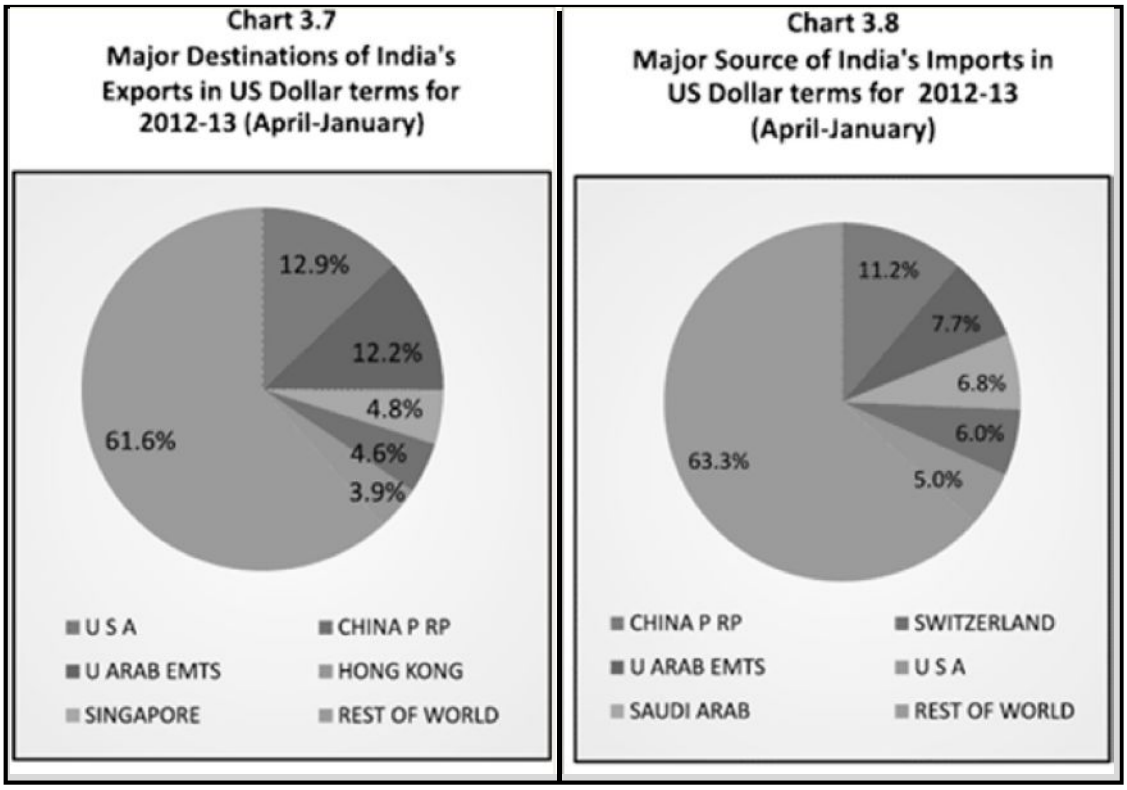
During 2012-13 (April–January), import of Coal, Coke & Briquettes decreased to US $ 13301.43 million from US $ 14851.58 million during the same period of last year, registering a negative growth of 10.44 per cent.

Gold & Silver

During 2012-13 (April–January) import of Gold and Silver decreased to US $ 46769.39 million from US $ 51751.03 million during the corresponding period of the previous year registering a negative growth of 9.63 per cent.

Direction of India's Foreign Trade

Share of major destinations of India's Exports and sources of Imports during 2012-13 (April– January) are given in Chart 3.7 and 3.8 respectively.



During the period 2012-13 (April–January), the share of Asia comprising of East Asia, ASEAN, West Asia, Other West Asia, North East Asia and South Asia accounted for 50.78 per cent of India's total exports in US $ terms. The share of Europe and America in India's exports stood at 18.88 per cent and 18.77 per cent respectively of which EU countries (27) comprises 16.99 per cent. During the period, USA (12.89 per cent) has been the most important country of export destination followed by UAE (12.20 per cent), Singapore (4.79 percent), China (4.59 per cent) and Hong Kong (3.95 per cent).

Asia accounted for 60.08 per cent of India's total imports during the period followed by Europe (17.39 per cent) and America (11.64 per cent). Among individual countries the share of China stood highest at (11.21 per cent) followed by UAE (7.67 per cent), Saudi Arabia (6.78 per cent), Switzerland (6.01 per cent) and USA (5.00 per cent).

Impact of Euro Zone crisis on India's Trade

The opening up of the Indian economy has greatly increased the role of trade. In the Eleventh Plan, the total share of merchandise exports and imports as a proportion of GDP rose from 36.4 per cent to 45.6 per cent.

However, along with the increased trade integration, the merchandise trade deficit too has risen from 7.8 per cent of GDP in 2007-08 to 10.6 per cent in 2011-12. This high trade deficit was offset by a growing net balance on service trade and a high level of remittances.

Following the global financial crisis in 2007-08, India's exports registered a 3.5% decline in 2009-10.The sovereign debt crisis in the Euro Zone periphery in 2011-12 impacted negatively economic growth in and exports from India. Between 2010-11 and 2011-12 India's growth rate declined from 8.4% in 2010-11 to 6.5% in 2011-12 and

to 5% during 2012-13. During the same period growth rate of exports declined from 40.5% in 2010-11 to 20.9% in 2011-12.The tight monetary policy has increased the cost of lending affecting domestic investment.

In sharp contrast to a rapid expansion witnessed both in India's exports and imports (21.3% and 32.3% respectively) in 2011-12, in 2012-13, exports have fallen month over month, even in absolute terms, since May, 2012. A negative growth in exports was recorded up to 5.5% in the first 9 months of this year, on a cumulative basis. However, since, January, 2013, exports have again started increasing, on a monthly basis.

As per DGCIS data, for the period April- January, 2013,as compared to April to January, 2012 the share of Europe in the entire export basket fell by 6.11% as against a growth of 15.7% for a corresponding period previous year.

The deepening of the Euro Area crisis has led to a considerably softer output growth in the major emerging market economies in as compared to a year earlier. The OECD Economic Outlook, 2012, mentions that: as the crisis has deepened, the volume of goods imported from India and South Africa by the Euro Area declined by 13-14% in the first half of 2012 than a year earlier.

The direct impact effect of the export declines over the year to the first half of 2012 corresponds to a hit to GDP growth over this period of around ¼ percentage point in India as per the OECD Economic Outlook, 2012. Besides, it is likely that there would be negative multiplier effects from the hit to exports, especially on investment. Weaker demand in the euro area will also have lowered exports of services to the Euro Area from these countries, a factor relatively important for India, and may also have had an indirect impact by reducing third-party demand for exports from the country.

Financial channels also have a relatively important role in the propagation of shocks. Heightened general risk aversion at times of intensified stress in the Euro Area places downward pressures on global equity prices and widens credit spreads, with negative effects on aggregate financial conditions. There was a sharp contraction in Euro Area banks' cross-border credit to emerging market economies in the latter half of 2011, when strains in euro area financial markets were very high, but little further change in the first quarter of 2012.

Presently, the euro crisis may now be acting as a relatively more important drag on growth, with further weakness in euro area domestic demand, and hence imports, set to persist into 2013, and macroeconomic policies in the major emerging market economies like India, now easing gradually and becoming less of a drag on growth.

Throughout the Eleventh Five Year Plan period Asia including ASEAN have been the most important destination for our exports having a share of around 50.76%, mainly due to high share of ASEAN and WANA. This is followed by Europe (18.96%) and America (16.42%) in April-March 2011-12. Exports to Africa remained stable around 8.1% (average from April-March 2007-08 to April-March 2011-12) with minor fluctuations during the course of the Eleventh Five Year Plan period. During the Eleventh Plan, Europe's share in the export basket fell from 22.86% in 2007-08 to 18.96% in 2011-12.

However, despite the global slowdown both in GDP growth and trade volumes, India recorded one of the highest export growths among the major trading nations of the world in 2011. WTO ranked India as the 19th largest merchandise exporter in the world, with a share of 1.7% of the global trade and the 12th largest importer with a share of 2.5% of global imports in 2011. In commercial services trade, India ranked higher: 8th largest exporter (3.3% of world exports) and 7th largest importer of services (3.1% of the global imports).

Trade flows within the South has increased substantially. However, the share of India, though increasing rapidly, is still much lower as compared to countries like China and those in South or South East Asia in particular. Thus, there is substantial potential for increasing India's trade with the South and with Latin America, Africa and CIS.

India has been pursuing a policy of market diversification directing her export promotion efforts at Asia and ASEAN, Latin America and Africa through Focus Market initiatives and bilateral trade agreements.

There are several important implications of the ongoing dynamic of change in the world economy which are relevant for India.

STATUS OF CURRENT ACCOUNT OF BALANCE OF PAYMENTS

Trade Deficit

The Trade deficit in April- January, 2013 was estimated at US $ 167.2 billion which was higher than the deficit of US $ 154.9 billion during April- January, 2012. This, coupled with the trend of falling surplus in services trade over the medium term, is likely to leave the current account deficit (CAD) too wide for comfort. CAD financing pressures can re-emerge in the face of event risks, although the recent policy measures announced by the government have helped boost portfolio inflows for now.

Foreign Direct Investment

FDI (Foreign Direct Investment) flows to India stood at US$ 22.2 billion during April-December 2012, which is 22.1 per cent lower than US$ 28.5 billion during April-December 2011. Up to December 2012, net FII (Foreign Institutional Investments) flows amounted to at US$ 16.0 billion (US$ 2.7 billion during the corresponding period of 2011-12). FII flows in recent months witnessed improvement, reflecting the impact of various reform measures announced by the Government.

Foreign Exchange Reserves

India's foreign exchange reserves comprise foreign currency assets (FCA), gold, special drawing rights (SDRs) and reserve tranche position (RTP) in the International Monetary Fund (IMF). The level of foreign exchange reserves is largely the outcome of the Reserve Bank of India (RBI) intervention in the foreign exchange market to smoothen exchange rate volatility and valuation changes due to movement of the US dollar against other major currencies of the world.

The foreign exchange reserves stood at US$ 304.8 billion at end March 2011. In the fiscal 2011-12, foreign exchange reserves reached a high of US$ 322.0 billion at end August, 2011. However, it declined thereafter and stood at US$ 294.4 billion at end March, 2012. In the current fiscal 2012-13, the foreign exchange reserves declined by US$ 4.7 billion to US$ 289.7 billion during the first quarter. At end- December 2012, reserves stood at US$ 295.6 billion, indicating a marginal increase of US$ 1.2 billion from US$ 294.4 billion at end-March, 2012. At this level, reserves provided about seven months of import cover.

Country-wise details of foreign exchange reserves reveal that India continues to be one of the largest holders of foreign exchange reserves. India is the eighth largest foreign exchange reserves holder in the world, after China, Japan, Russia, Switzerland, Brazil, Republic of Korea and China P R Hong Kong at end December, 2012.

Way Ahead

The initial shift from a current account surplus to a deficit situation accompanied the transition of the Indian economy's growth to a higher gear and the parallel dramatic rise in the investment rate. A sharp deterioration of the merchandise trade deficit to GDP ratio by over 5 percentage points between 2004-05 and 2011-12 (from 4.3% to 10.6%), as imports grew faster than even fast growing exports, was chiefly responsible. While oil imports did increase during this period, it was imports of manufactured products which were the main driver of the rapid increase in imports before the global crisis erupted. The impact on the current account of the trends in merchandise trade was, however, moderated somewhat by a simultaneous rise in India's invisibles surplus, to which growth of software services exports and private remittances were the principal contributors.

However, Indian exports of both goods and services increased substantially faster during the pre-crisis phase of high growth, even if India's merchandise trade deficit eventually worsened on account of rapid growth of imports.

The surge in exports also began before growth picked up. This was accompanied by significant changes in both the direction of Indian exports of goods, as well as, in its product composition. Indian exports benefited from the generally positive growth scenario of many developing and oil producing countries and the share of these countries in Indian exports increased quite sharply. This process was not driven by 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 – involved greater requirements of capital per unit of output 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 from 2003-04.

Since imports eventually outpaced exports, even in the very same categories of products whose share in Indian exports was rising, if the trend in merchandise trade had been all that was there, the high growth would have been hard to sustain even for the period that it did. The parallel growth of India's services exports as well as the large inflow of remittances, also therefore played an important role. In particular by checking the expansion of the current account deficit, they were critical to maintaining the conditions necessary for the large capital inflows that occurred as part of a worldwide trend.

There is now an increasing shift in India's trade from conventional destinations i.e. US and EU to the South Asia, ASEAN, Africa and Latin America. China has become the largest trade partner, however, the accompanying development of trade deficit is worrying.

Expansion of trade basket and diversification of markets will improve the balance of trade. Export expansion needs to be accompanied by contraction in some of the high volume high value imports that display inelastic tendencies.

Thus, in an increasingly inter-connected world, no country can remain isolated from what happens in the other parts of the world. Seeking new markets is the only realistic option that India has in the present circumstances. The government and the private sector will have to work in tandem to identify the measures that are needed to promote exports.

Note : Recent trends in global trade and India's foreign trade is given for students reference. The students should keep themselves updated from various other sources. They can refer to World Trade Report, Economic Survey of India etc. to know the recent trend.

REGIONAL ECONOMIC INTEGRATION

Regional economic integration has enabled countries to focus on issues that are relevant to their stage of development as well as encourage trade between neighbors. Regional integration is a process in which states enter into a regional agreement in order to enhance regional cooperation through regional institutions and rules. The objectives of the agreement could range from economic to political to environmental, although it has typically taken the form of a political economy initiative where commercial interests have been the focus for achieving broader socio-political and security objectives, as defined by national governments. Regional integration has been organized either via supranational institutional structures or through intergovernmental decision-making, or a combination of both.

Past efforts at regional integration have often focused on removing barriers to free trade in the region, increasing the free movement of people, labor, goods, and capital across national borders, reducing the possibility of regional armed conflict (for example, through Confidence and Security-Building Measures), and adopting cohesive regional stances on policy issues, such as the environment, climate change and migration.

Intra-regional trade refers to trade which focuses on economic exchange primarily between countries of the same region or economic zone. In recent years countries within economic-trade regimes such as ASEAN in Southeast Asia have increased the level of trade and commodity exchange between themselves which reduces the inflation and tariff barriers associated with foreign markets resulting in growing prosperity

REGIONAL TRADING BLOCS

A trade bloc is a type of intergovernmental agreement, often part of a regional intergovernmental organization, where regional barriers to trade, (tariffs and non-tariff barriers) are reduced or eliminated among the participating states. A regional trading bloc is a group of countries within a geographical region that protect themselves from imports from non-members. A trade bloc is basically a free-trade zone, or near-free-trade zone, formed by one or more tax, tariff, and trade agreements between two or more countries. Trading blocs are a form of economic integration, and increasingly shape the pattern of world trade.

Regional trade blocks promote trade within the block and defend its members against global competition. Defense against global competition is obtained through established tariffs on goods produced by member states, import quotas, government subsidies, onerous bureaucratic import processes, and technical and other non-tariff barriers. Since trade is not an isolated activity, member states within regional blocks also cooperate in economic, political, security, climatic, and other issues affecting the region. Members of successful trade blocs usually share four common traits: similar levels of per capita GNP, geographic proximity, similar or compatible trading regimes, and political commitment to regional organization.

Advocates of worldwide free trade are generally opposed to trading blocs, which, they argue, encourage regional trade as opposed to global free trade.

TYPES OF REGIONAL TRADING BLOCS

Trade blocs can be stand-alone agreements between several states (such as the North American Free Trade Agreement (NAFTA) or part of a regional organization (such as the European Union). Depending on the level of economic integration, trade blocs can fall into six different categories, such as preferential trading areas, free trade areas, customs unions, common markets, economic union and monetary unions , and political union .

1. Preferential Trade Area : Preferential Trade Areas (PTAs) exist when countries within a geographical region agree to reduce or eliminate tariff barriers on selected goods imported from other members of the area. This is often the first small step towards the creation of a trading bloc.

2. Free trade area : Free Trade Areas (FTAs) are created when two or more countries in a region agree to reduce or eliminate barriers to trade on all goods coming from other members. This is the most basic form of economic cooperation. Member countries remove all barriers to trade between themselves but are free to independently determine trade policies with nonmember nations. An example is the North American Free Trade Agreement (NAFTA).

3. Customs union : This type provides for economic cooperation as in a free-trade zone. Barriers to trade are removed between member countries. The primary difference from the free trade area is that members agree to treat trade with non-member countries in a similar manner. A customs union involves the removal of tariff barriers between members, plus the acceptance of a common (unified) external tariff against non-members. This means that members may negotiate as a single bloc with third parties, such as with other trading blocs, or with the WTO. The Gulf Cooperation Council (GCC) Cooperation Council for the Arab States of the Gulf is an example.

4. Common market: A ‘common market’ is the first significant step towards full economic integration, and occurs when member countries trade freely in all economic resources – not just tangible goods. This means that all barriers to trade in goods, services, capital, and labor are removed. In addition, as well as removing tariffs, non-tariff barriers are also reduced and eliminated. For a common market to be successful there must also be a significant level of harmonization of micro-economic policies, and common rules regarding monopoly power and other anti-competitive practices. There may also be common policies affecting key industries, such as the Common Agricultural Policy (CAP) and Common Fisheries Policy (CFP) of the European Single Market (ESM). This type allows for the creation of economically integrated markets between member countries. Trade barriers

are removed, as are any restrictions on the movement of labor and capital between member countries. Like customs unions, there is a common trade policy for trade with nonmember nations. The primary advantage to workers is that they no longer need a visa or work permit to work in another member country of a common market. An example is the Common Market for Eastern and Southern Africa (COMESA).

5. Economic and Monetary union: This type is created when countries enter into an economic agreement to remove barriers to trade and adopt common economic policies. An example is the European Union (EU). Monetary union is a type of trade bloc which is composed of an economic union (common market and customs union) with a monetary union. Monetary union is established through a currency-related trade pact. An intermediate step between pure monetary union and a complete economic integration is the fiscal union. Economic and Monetary Union of the European Union with the Euro for the Euro-zone members is the example of monetary union.

6. Political union: In order to be successful the more advanced integration steps are typically accompanied by unification of economic policies (tax, social welfare benefits, etc.), reductions in the rest of the trade barriers, introduction of supranational bodies, and gradual moves towards the final stage, a "political union". Political union is the final stage in economic integration with more formal political links between the countries. A limited form of political union may exist when two or more countries share common decision making bodies and have common policies. It is the unification of previously separate nations. The unification of West and East Germany in 1990 is an example of total political union.

ADVANTAGES OF REGIONAL TRADING BLOCS

1. Free trade within the bloc: Knowing that they have free access to each other's markets, members are encouraged to specialise. This means that, at the regional level, there is a wider application of the principle of comparative advantage.

2. Market access and trade creation: Easier access to each other's markets means that trade between members is likely to increase. *Trade creation* exists when free trade enables high cost domestic producers to be replaced by lower cost, and more efficient imports. Because low cost imports lead to lower priced imports, there is a 'consumption effect', with increased demand resulting from lower prices. These agreements create more opportunities for countries to trade with one another by removing the barriers to trade and investment. Due to a reduction or removal of tariffs, cooperation results in cheaper prices for consumers in the bloc countries. Studies indicate that regional economic integration significantly contributes to the relatively high growth rates in the less-developed countries.

3. Economies of scale: Producers can benefit from the application of scale economies, which will lead to lower costs and lower prices for consumers.

4. Jobs: Jobs may be created as a consequence of increased trade between member economies. By removing restrictions on labor movement, economic integration can help expand job opportunities.

5. Protection: Firms inside the bloc are protected from cheaper imports from outside, such as the protection of the EU shoe industry from cheap imports from China and Vietnam.

6. Consensus and cooperation: Member nations may find it easier to agree with smaller numbers of countries. Regional understanding and similarities may also facilitate closer political cooperation.

DISADVANTAGES OF REGIONAL TRADING BLOCS

1. Loss of benefits: The benefits of free trade between countries in different blocs is lost.

2. Distortion of trade: Trading blocs are likely to distort world trade, and reduce the beneficial effects of specialisation and the exploitation of *comparative advantage*.

3. Inefficiencies and trade diversion: Inefficient producers within the bloc can be protected from more efficient ones outside the bloc. For example, inefficient European farmers may be protected from low-cost imports from

developing countries. *Trade diversion* arises when trade is diverted away from efficient producers who are based outside the trading area. The flip side to trade creation is trade diversion. Member countries may trade more with each other than with nonmember nations. This may mean increased trade with a less efficient or more expensive producer because it is in a member country. In this sense, weaker companies can be protected inadvertently with the bloc agreement acting as a trade barrier. In essence, regional agreements have formed new trade barriers with countries outside of the trading bloc.

4. Retaliation: The development of one regional trading bloc is likely to stimulate the development of others. This can lead to trade disputes, such as those between the EU and NAFTA, including the recent Boeing (US)/ Airbus (EU) dispute. The EU and US have a long history of trade disputes, including the dispute over US steel tariffs, which were declared illegal by the WTO in 2005. In addition, there are the so-called *beef wars* with the US applying £60m tariffs on EU beef in response to the EU's ban on US beef treated with hormones; and complaints to the WTO of each other's generous agricultural support. During the 1970s many former UK colonies formed their own trading blocs in reaction to the UK joining the European common market.

5. Employment shifts and reductions: Countries may move production to cheaper labor markets in member countries. Similarly, workers may move to gain access to better jobs and wages. Sudden shifts in employment can tax the resources of member countries.

6. Loss of national sovereignty: With each new round of discussions and agreements within a regional bloc, nations may find that they have to give up more of their political and economic rights. The economic crisis in Greece is threatening not only the EU in general but also the rights of Greece and other member nations to determine their own domestic economic policies.

IMPORTANT REGIONAL TRADING BLOCKS

There are more than one hundred regional trade agreements in place, a number that is continuously evolving as countries reconfigure their economic and political interests and priorities. Additionally, the expansion of the World Trade Organization (WTO) has caused smaller regional agreements to become obsolete. Some of the regional blocs also created side agreements with other regional groups leading to a web of trade agreements and understandings.

1. ASSOCIATION OF SOUTH-EAST ASIAN NATIONS (ASEAN)

ASEAN is the most prominent regional grouping in Asia. The Association of Southeast Asian Nations is a geo-political and economic organization of ten countries located in Southeast Asia, which was formed on 8 August 1967 by Indonesia, Malaysia, the Philippines, Singapore and Thailand. Since then, membership has expanded to include Brunei, Burma (Myanmar), Cambodia, Laos, and Vietnam. Its aims include accelerating economic growth, social progress, and cultural development among its members, protection of regional peace and stability, and opportunities for member countries to discuss differences peacefully.

ASEAN covers a land area of 4.46 million km², which is 3% of the total land area of Earth, and has a population of approximately 600 million people, which is 8.8% of the world's population. The sea area of ASEAN is about three times larger than its land counterpart. In 2011, its combined nominal GDP had grown to more than US$ 2 trillion. If ASEAN were a single entity, it would rank as the eighth largest economy in the world.

ASEAN has emphasized regional cooperation on the three pillars of security and socio-cultural and economic integration. It has made most progress in economic integration and aims to create an ASEAN Economic Community (AEC) by 2015.

The foundation of the AEC is the ASEAN Free Trade Area (AFTA), a common external preferential tariff scheme to promote the free flow of goods within ASEAN. Other elements of economic integration, such as the free flow of investment and services and the elimination of non-tariff barriers, have been added by the ASEAN leaders.

Aims and Purposes

As set out in the ASEAN Declaration, the aims and purposes of ASEAN are:

1. To accelerate the economic growth, social progress and cultural development in the region through joint endeavours in the spirit of equality and partnership in order to strengthen the foundation for a prosperous and peaceful community of Southeast Asian Nations;
2. To promote regional peace and stability through abiding respect for justice and the rule of law in the relationship among countries of the region and adherence to the principles of the United Nations Charter;
3. To promote active collaboration and mutual assistance on matters of common interest in the economic, social, cultural, technical, scientific and administrative fields;
4. To provide assistance to each other in the form of training and research facilities in the educational, professional, technical and administrative spheres;
5. To collaborate more effectively for the greater utilisation of their agriculture and industries, the expansion of their trade, including the study of the problems of international commodity trade, the improvement of their transportation and communications facilities and the raising of the living standards of their peoples;
6. To promote Southeast Asian studies; and
7. To maintain close and beneficial cooperation with existing international and regional organisations with similar aims and purposes, and explore all avenues for even closer cooperation among themselves.

Fundamental Principles

In their relations with one another, the ASEAN Member States have adopted the following fundamental principles, as contained in the Treaty of Amity and Cooperation in Southeast Asia (TAC) of 1976:

1. Mutual respect for the independence, sovereignty, equality, territorial integrity, and national identity of all nations;
2. The right of every State to lead its national existence free from external interference, subversion or coercion;
3. Non-interference in the internal affairs of one another;
4. Settlement of differences or disputes by peaceful manner;
5. Renunciation of the threat or use of force; and
6. Effective cooperation among themselves.

Asean Charter

The ASEAN Charter serves as a firm foundation in achieving the ASEAN Community by providing legal status and institutional framework for ASEAN. It also codifies ASEAN norms, rules and values; sets clear targets for ASEAN; and presents accountability and compliance. The ASEAN Charter entered into force on 15 December 2008. It is a legally binding agreement among the 10 ASEAN Member States.

Through agreements such as the ASEAN Charter, ASEAN's leaders are attempting to build a single market, but without either a strong central executive (comparable to the European Commission in the European Union) or a well-developed body of laws and dispute settlement mechanisms (like those of the North American Free Trade Association (NAFTA)). ASEAN members' historical reluctance to encourage either of these elements stems from a fear of impinging on ASEAN's long-held principles of non-interference and consensus. However, failure to integrate ASEAN's diverse markets will mean a loss of investment and economic opportunities to regional competitors, such as China and India. This tension between the need to integrate and the reluctance to yield national sovereignty is the main factor affecting the development of the AEC.

ASEAN Structure

The supreme authority in ASEAN is the ASEAN Summit of national leaders. Decisions made at the summit are intended to represent a consensus among the ASEAN nations, although the legal authority of such decisions has not been tested. Summit meetings have been held annually, but the charter foresees meetings twice a year, along with special meetings when necessary. The chairmanship rotates among the members every year by alphabetical order. The charter establishes councils at ministerial level to handle substantive matters. The ASEAN Economic Community Council, formerly known as the ASEAN Economic Ministers meeting, meet twice yearly and coordinate the development of the AEC. The council is supported by the Senior Economic Officials Meeting, a grouping of national-level bureaucrats that meets between the council meetings. The charter also requires each member to station a permanent representative in Jakarta. A committee of permanent representatives liaise with the secretariat, ministerial councils and national secretariats to establish within the members' national governments. The ASEAN Secretariat provides administrative support to ASEAN. The staffs of the secretariat are hired competitively on fixed-term contracts. The secretary general heads the secretariat and is appointed for a five-year term is mandated to initiate, advise, coordinate, and implement ASEAN activities.. The nationality of the secretary general also rotates based on alphabetical order. The members of the professional staff of the ASEAN Secretariat are appointed on the principle of open recruitment and region-wide competition. ASEAN has several specialized bodies and arrangements promoting inter-governmental cooperation in various fields. In addition, ASEAN promotes cooperative activities with organizations having related aims and purposes. Furthermore, there are Non-Governmental Organizations (NGOs), which have formal affiliations with ASEAN.

2. EUROPEAN UNION

The EU is the world's largest trading bloc, and second largest economy, after the USA. The European Union (EU) is an economic and political union of 27 member states that are located primarily in Europe. The EU operates through a system of supranational independent institutions and intergovernmental negotiated decisions by the member states. Institutions of the EU include the European Commission, the Council of the European Union, the Court of Justice of the European Union, the European Central Bank, the Court of Auditors, and the European Parliament. The European Parliament is elected every five years by EU citizens. The EU's de facto capital is Brussels.

The EU was originally called the Economic Community (*Common Market*, or *The Six*) after its formation following the Treaty of Rome in 1957. The original six members were Germany, France, Italy, Belgium, Netherlands, and Luxembourg. The term 'European Communities' is a collective term for the European Coal and Steel Community (ECSC), founded in 1951, the European Economic Community (EEC) and the European Atomic Energy Community (EURATOM or EAEC), founded in 1957. The European Union, created by the Maastricht Treaty, did not make the European Communities disappear. They form its institutional framework. The Union remain based on the Communities, supplemented by the policies and the forms of cooperation - Economic and Monetary Fund, Common Foreign and Security Policy, cooperation in justice and home affairs brought in by that treaty. The latest major amendment to the constitutional basis of the EU, the Treaty of Lisbon, came into force in 2009.

The EU has developed a single market through a standardised system of laws that apply in all member states. Within the Schengen Area (which includes 22 EU and 4 non-EU states) passport controls have been abolished. EU policies aim to ensure the free movement of people, goods, services, and capital, enact legislation in justice and home affairs, and maintain common policies on trade, agriculture, fisheries and regional development.

A monetary union, the eurozone, was established in 1999 and is composed of 17 member states. Through the Common Foreign and Security Policy the EU has developed a role in external relations and defence. Permanent diplomatic missions have been established around the world. The EU is represented at the United Nations, the WTO, the G8 and the G-20.

With a combined population of over 500 million inhabitants, or 7.3% of the world population, the EU, in 2012,

generated a nominal gross domestic product (GDP) of 16.584 trillion US dollars, representing approximately 20% of the global GDP when measured in terms of purchasing power parity, and represents the largest nominal GDP and GDP PPP in the world. The EU was the recipient of the 2012 Nobel Peace Prize.

The EU has following 27 members:

Austria	Germany	Norway
Belgium	Greece	Poland
Bulgaria	Ireland	Portugal
Cyprus	Italy	Romania
Czech Republic	Latvia	Spain
Denmark	Lithuania	Slovenia
Estonia	Luxembourg	Slovakia
Finland	Malta	Sweden
France	Netherlands	UK

The initial aim was to create a single market for goods, services, capital, and labour by eliminating barriers to trade and promoting free trade between members. Some **examples of the role** the European Union plays around the world are given below:

- The EU promotes peace and reconciliation through its political, practical and economic support.
- **It provides development aid** which is making a huge difference to millions of people's livelihoods around the world.
- The Union is committed to **human rights** and works to ensure they are respected universally.
- The Union works closely with the **United Nations** on a host of issues.
- It supports in **building security around the world through its** Common Security and Defence Policy (CSDP).
- The European Union is the world's largest trading bloc. Trade is a common policy so the EU speaks with a single voice in trade negotiations with international partners in promoting a free and fairer international trading system.

The European Union (EU) has four main institutions namely through which it functions, the Council of Ministers, the European Commission, the European Parliament and the European Court of Justice. Other bodies such as the Economic and Social Committee and the Committee of the Regions have particular roles to play in the decision making process.

The Council of Minister

The Council is the EU's main decision-making body. It is the embodiment of the Member States, whose representatives it brings together regularly at ministerial level. The Council is comprised of ministers from national governments of each of the member states. It meets mostly in Brussels or Luxembourg to deliberate upon legislation and policy. Diplomats and officials in a committee called Coreper, involving the permanent representations to the EU of each member state, prepare the Council's work. The United Kingdom Permanent Representation is known as UKRep.

The Presidency of the Council is held by each member state, in rotation, for a period of six months. The country holding the presidency hosts a meeting of the heads of states and governments every six months, known as the European Council.

The Council has following major responsibilities:

1. It is the Union's legislative body; for a wide range of EU issues, it exercises that legislative power in co-decision with the European Parliament;
2. It coordinates the broad economic policies of the Member States;
3. It concludes, on behalf of the EU, international agreements with one or more States or international organisations;
4. It shares budgetary authority with Parliament;
5. It takes the decisions necessary for framing and implementing the common foreign and security policy, on the basis of general guidelines established by the European Council;
6. It coordinates the activities of Member States and adopts measures in the field of police and judicial cooperation in criminal matters.

The European Commission

The EU's Administrative & Executive body is headed by the Twenty Commissioners who are charged with furthering the goals of the Union and implementing EU policy and legislation. The Commission for consideration and decision by the Council of Ministers and the European Parliament drafts initial proposals for legislation and policy. The Commissioners, who serve for five years, are nominated by national governments and approved by the European Parliament. MEPs have the power to sack the Commission. The headquarters of the Commission is in Brussels.

The Commission is the driving force in the Union's institutional system:

1. It has the right to initiate draft legislation and therefore presents legislative proposals to Parliament and the Council;
2. As the Union's executive body, it is responsible for implementing the European legislation (directives, regulations, decisions), budget and programmes adopted by Parliament and the Council;
3. It acts as guardian of the Treaties and, together with the Court of Justice, ensures that Community law is properly applied;
4. It represents the Union on the international stage and negotiates international agreements, chiefly in the field of trade and cooperation.

The European Parliament

The European Parliament is the democratically elected body whose 626 members (MEPs) are elected every five years. Working in Brussels and Strasbourg, Parliament scrutinises the activities of other EU institutions, passes the annual EU budget, and shapes and decides new legislation jointly with the Council of Ministers. The Parliament has a staff of 3,850.

Elected every five years by direct universal suffrage, the European Parliament is the expression of the democratic will of the Union's 498 million citizens. Brought together within pan-European political groups, the major political parties operating in the Member States are represented.

The Parliament has three essential functions:

1. It shares with the Council the power to legislate, i.e. to adopt European laws (directives, regulations, decisions). Its involvement in the legislative process helps to guarantee the democratic legitimacy of the texts adopted;
2. It shares budgetary authority with the Council, and can therefore influence EU spending. At the end of the procedure, it adopts the budget in its entirety;

3. It exercises democratic supervision over the Commission. It approves the nomination of Commissioners and has the right to censure the Commission. It also exercises political supervision over all the institutions.

The European Court of Justice

Based in Luxembourg, the Court, which has a judge from each member state, adjudicates on all legal issues and disputes involving Community law. The judges, who sit for a period of six years, are assisted by nine advocates-general who give a preliminary ruling on each case before a final judgement. The Court deals with two main types of actions: those referred to it by national courts for rulings of interpretation of Community law; and those started by one of the other institutions (usually the Commission against a member state).

3. NORTH AMERICAN FREE TRADE AGREEMENT (NAFTA)

The North American Free Trade Agreement (NAFTA) is a comprehensive trade agreement that sets the rules of trade and investment between Canada, the United States, and Mexico. Since the agreement entered into force on January 1, 1994, NAFTA has systematically eliminated most tariff and non-tariff barriers to free trade and investment between the three NAFTA countries.

- NAFTA is a formal agreement that establishes clear rules for commercial activity between Canada, the United States, and Mexico. NAFTA is overseen by a number of institutions that ensure the proper interpretation and smooth implementation of the Agreement's provisions.
- Since NAFTA came into effect, trade and investment levels in North America have increased, bringing strong economic growth, job creation, and better prices and selection in consumer goods. North American businesses, consumers, families, workers, and farmers have all benefited. For more information about NAFTA's many benefits, please see: Results: North Americans Are Better Off After 15 years of NAFTA.
- NAFTA provides North American businesses with better access to materials, technologies, investment capital, and talent available across North America.
- Each NAFTA country forgoes tariffs on imported goods "originating" in the other NAFTA countries. Rules of origin enable customs officials to decide which goods qualify for this preferential tariff treatment under NAFTA. The negotiators of the Agreement sought to make the rules of origin very clear so as to provide certainty and predictability to producers, exporters, and importers. They also sought to ensure that NAFTA's benefits are not extended to goods imported from non-NAFTA countries that have undergone only minimal processing in North America.
- The procedures for presenting a claim to each NAFTA partner are different. To certify that goods qualify for the preferential tariff treatment under NAFTA, the exporter must complete a certificate of origin. A producer or manufacturer may also complete a certificate of origin to be used as a basis for an exporter's certificate of origin. To make a claim for NAFTA preference, the importer must possess a certificate of origin at the time the claim is made.
- Four categories of travelers are eligible for temporary entry from one NAFTA country into another: business visitors, traders and investors, intra-company transferees, and professionals.
- On January 1, 2008, the last remaining tariffs were removed within North America. When implemented, NAFTA immediately lifted tariffs on the majority of goods produced by the NAFTA partners and called for the phased elimination, over 15 years, of most remaining barriers to cross-border investment and to the movement of goods and services between the three countries.

Objectives of NAFTA :

- eliminate barriers to trade in, and facilitate the cross-border movement of goods and services between the territories of the Parties;

- promote conditions of fair competition in the free trade area;
- increase substantially investment opportunities in the territories of the Parties;
- provide adequate and effective protection and enforcement of intellectual property rights in each Party's territory;
- create effective procedures for the implementation and application of this Agreement, for its joint administration and for the resolution of disputes; and
- establish a framework for further trilateral, regional and multilateral cooperation to expand and enhance the benefits of this Agreement.

NAFTA has been a remarkable success story for all three partners. It has contributed to significant increases in trade and investment flows between Canada, the United States, and Mexico. It has benefited companies in all three countries, paving the way for increased sales, new partnerships, and new opportunities. In this section, we explore the innovative ways in which companies have been able to expand their presence in the North American continent.

Structure of NAFTA

A number of NAFTA institutions work to ensure smooth implementation and day-to-day oversight of the Agreement's provisions.

(a) Free Trade Commission:

- Made up of ministerial representatives from the NAFTA partners.
- Supervises the implementation and further elaboration of the Agreement and helps resolve disputes arising from its interpretation.
- Oversees the work of the NAFTA committees, working groups, and other subsidiary bodies.

(b) NAFTA Coordinators

- Senior trade department officials designated by each country.
- Responsible for the day-to-day management of NAFTA implementation.

(c) NAFTA Working Groups and Committees

- Over 30 working groups and committees have been established to facilitate trade and investment and to ensure the effective implementation and administration of NAFTA.
- Key areas of work include trade in goods, rules of origin, customs, agricultural trade and subsidies, standards, government procurement, investment and services, cross-border movement of business people, and alternative dispute resolution.

(d) NAFTA Secretariat: The NAFTA Secretariat is an independent agency that is responsible for the impartial administration of the dispute settlement provisions of the North American Free Trade Agreement. It has a Canadian, a Mexican, and a United States Section, each headed by a national Secretary, and with offices in each national capital. The Secretariat is accountable to the NAFTA Free Trade Commission, which comprises the ministers responsible for international trade in the three NAFTA partner countries. It is also responsible for administering the dispute settlement provisions of the Agreement and for administering dispute resolution processes. It maintains a court-like registry relating to panel, committee, and tribunal proceedings. It also maintains a tri-national website containing up-to-date information on past and current disputes.

(e) Commission for Labor Cooperation

- Created to promote cooperation on labor matters among NAFTA members and the effective enforcement of domestic labor law.
- Consists of a Council of Ministers (comprising the labor ministers from each country) and a Secretariat, which provides administrative, technical, and operational support to the Council and implements an annual work program. Departments responsible for labor in each of the three countries serve as domestic implementation points.

(f) Commission for Environmental Cooperation

- Established to further cooperation among NAFTA partners in implementing the environmental side accord to NAFTA and to address environmental issues of continental concern, with particular attention to the environmental challenges and opportunities presented by continent-wide free trade.
- Consists of a Council (comprising the environment ministers from each country), a Joint Public Advisory Committee (a 15-member, independent volunteer body that provides advice and public input to Council on any matter within the scope of the environmental accord), and a Secretariat (which provides administrative, technical, and operational support).

4. SOUTH ASIAN ASSOCIATION FOR REGIONAL COOPERATION (SAARC)

The South Asian Association for Regional Cooperation (SAARC) is an organisation of South Asian nations, which was established on 8 December 1985 when the government of Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan, and Sri Lanka formally adopted its charter providing for the promotion of economic and social progress, cultural development within the South Asia region and also for friendship and cooperation with other developing countries. It is dedicated to economic, technological, social, and cultural development emphasising collective self-reliance.

Its seven founding members are Sri Lanka, Bhutan, India, Maldives, Nepal, Pakistan, and Bangladesh. Afghanista joined the organisation in 2007.

Meetings of heads of state are usually scheduled annually; meetings of foreign secretaries, twice annually. It is headquartered in Kathmandu, Nepal.

The main goal of the Association is to accelerate the process of economic and social development in member states, through joint action in the agreed areas of cooperation.

The idea of regional cooperation in South Asia was first mooted in November 1980. After consultations, the Foreign Secretaries of the seven countries met for the first time in Colombo, in April 1981. This was followed, a few months later, by the meeting of the Committee of the Whole, which identified five broad areas for regional cooperation. The Foreign Ministers, at their first meeting in New Delhi, in August 1983, formally launched the Integrated Programme of Action (IPA) through the adoption of the Declaration on South Asian Regional Cooperation (SARC). At the First Summit held in Dhaka on 7-8 December 1985, the Charter establishing the South Asian Association for Regional Cooperation (SAARC) was adopted.

Objectives

The objectives, principles and general provisions, as mentioned in the SAARC Charter, are as follows:

- To promote the welfare of the peoples of South Asia and to improve their quality of life;
- To accelerate economic growth, social progress and cultural development in the region and to provide all individuals the opportunity to live in dignity and to realise their full potentials;
- To promote and strengthen collective self-reliance among the countries of South Asia;

- To contribute to mutual trust, understanding and appreciation of one another's problems;
- To promote active collaboration and mutual assistance in the economic, social, cultural, technical and scientific fields;
- To strengthen cooperation with other developing countries;
- To strengthen cooperation among themselves in international forums on matters of common interests; and
- To cooperate with international and regional organizations with similar aims and purposes.

Principles

The principles are as follows

- Respect for sovereignty, territorial integrity, political equality and independence of all members states
- Non-interference in the internal matters is one of its objectives
- Cooperation for mutual benefit
- All decisions to be taken unanimously and need a quorum of all eight members
- All bilateral issues to be kept aside and only multilateral(involving many countries) issues to be discussed without being prejudiced by bilateral issues.

SAARC Secretariat

Secretariat of the South Asian Association for Regional Cooperation is in Kathmandu, Nepal. It is headed by the Secretary General appointed by the Council of Ministers from Member Countries in an alphabetical order for a three-year term. He is assisted by the Professional and the General Service Staff, and also an appropriate number of functional units called Divisions assigned to Directors on deputation from Member States. The Secretariat coordinates and monitors implementation of activities, prepares for and services meetings, and serves as a channel of communication between the Association and its Member States as well as other regional organisations.

The Memorandum of Understanding on the establishment of the Secretariat which was signed by Foreign Ministers of member countries on 17 November 1986 at Bangalore, India contains various clauses concerning the role, structure and administration of the SAARC Secretariat as well as the powers of the Secretary-General.

In several recent meetings the heads of state or government of member states of SAARC have taken some important decisions and bold initiatives to strengthen the organisation and to widen and deepen regional co-operation.

The SAARC Secretariat and Member States observe 8 December as the SAARC Charter Day1.

The highest authority of the Association rests with the Heads of State or Government.

Council of Ministers

Comprising of the Foreign Ministers of member states it is responsible for the formulation of policies; reviewing progress; deciding on new areas of cooperation; establishing additional mechanisms as deemed necessary; and deciding on other matters of general interest to the Association. The Council meets twice a year and may also meet in extraordinary session by agreement of member states.

Standing Committee

Comprising of the Foreign Secretaries of member states it is entrusted with the overall monitoring and coordination of programmes and the modalities of financing; determining inter-sectoral priorities; mobilising regional and

external resources; and identifying new areas of cooperation based on appropriate studies. It may meet as often as deemed necessary but in practice it meets twice a year and submits its reports to the Council of Ministers.

Programming Committee

Comprising of the senior officials it meets prior to the Standing Committee sessions to scrutinize Secretariat Budget, finalise the Calendar of Activities and take up any other matter assigned to it by the Standing Committee.

Technical Committees

Comprising of representatives of member states, they formulate programmes and prepare projects in their respective fields. They are responsible for monitoring the implementation of such activities and report to the Standing Committee. The Chairmanship of each Technical Committee normally rotates among member countries in alphabetical order, every two years.

Action Committees

According to the SAARC Charter, there is a provision for Action Committees comprising member states concerned with implementation of projects involving more than two, but not all member states.

5. SOUTH ASIAN PREFERENTIAL TRADING AREA

In December 1991, the Sixth Summit of SAARC held in Colombo approved the establishment of an Inter-Governmental Group (IGG) to formulate an agreement to establish a SAARC Preferential Trading Arrangement (SAPTA) by 1997. The Heads of State or Government approved the establishment of an Intergovernmental Group (IGG) to seek agreement on an institutional framework under which specific measures for trade liberalization among SAARC member states could be furthered. IGG evolved a draft Agreement on SAARC Preferential Trading Arrangement (SAPTA) during its first two Meetings. The Agreement on SAPTA was signed on 11 April 1993 and entered into force on 7 December 1995 well in advance of the date stipulated by the Colombo Summit. The Agreement reflected the desire of the Member States to promote and sustain mutual trade and economic cooperation within the SAARC region through the exchange of concessions.

The basic principles underlying SAPTA are:

- overall reciprocity and mutuality of advantages so as to benefit equitably all Contracting States, taking into account their respective level of economic and industrial development, the pattern of their external trade, and trade and tariff policies and systems;
- negotiation of tariff reform step by step, improved and extended in successive stages through periodic reviews;
- recognition of the special needs of the Least Developed Contracting States and agreement on concrete preferential measures in their favour; and
- inclusion of all products, manufactures and commodities in their raw, semi-processed and processed forms.

Four rounds of trade negotiations have been concluded under SAPTA covering over 5000 commodities. Each Round contributed to an incremental trend in the product coverage and the deepening of tariff concessions over previous Round

6. SOUTH ASIAN FREE TRADE AREA (SAFTA)

SAPTA was envisaged primarily as the first step towards the transition to a South Asian Free Trade Area (SAFTA) leading subsequently towards a Customs Union, Common Market and Economic Union.

In 1995, the Sixteenth session of the Council of Ministers (New Delhi, 18-19 December 1995) agreed on the

need to strive for the realization of SAFTA and to this end an Inter-Governmental Expert Group (IGEG) was set up in 1996 to identify the necessary steps for progressing to a free trade area.

The Tenth SAARC Summit (Colombo, 29-31 July 1998) decided to set up a Committee of Experts (COE) to draft a comprehensive treaty framework for creating a free trade area within the region, taking into consideration the asymmetries in development within the region and bearing in mind the need to fix realistic and achievable targets.

The SAFTA Agreement was signed on 6 January 2004 during Twelfth SAARC Summit held in Islamabad, Pakistan. The Agreement entered into force on 1 January 2006, and the Trade Liberalization Programme commenced from 1st July 2006.

The purpose of SAFTA is to encourage and elevate common contract among the countries such as medium and long term contracts. Contracts involving trade operated by states, supply and import assurance in respect of specific products etc. It involves agreement on tariff concession like national duties concession and non-tariff concession.

It created a free trade area of 1.6 billion people in Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri Lanka. The seven foreign ministers of the region signed a framework agreement on SAFTA to reduce customs duties of all traded goods to zero by the year 2016.

SAFTA requires the developing countries in South Asia (India, Pakistan and Sri Lanka) to bring their duties down to 20 percent in the first phase of the two-year period ending in 2007. In the final five-year phase ending 2012, the 20 percent duty will be reduced to zero in a series of annual cuts. The least developed nations in South Asia (Nepal, Bhutan, Bangladesh, Afghanistan and Maldives) have an additional three years to reduce tariffs to zero. India and Pakistan ratified the treaty in 2009, whereas Afghanistan as the 8th member state of the SAARC ratified the SAFTA protocol on the 4th of May 2011.

Following the Agreement coming into force the SAFTA Ministerial Council (SMC) has been established comprising the Commerce Ministers of the Member States. To assist the SMC, a SAFTA Committee of Experts (SCOE) has been formed. SCOE is expected to submit its report to SMC every six months. The SAFTA Agreement states that the “the SMC shall meet at least once every year or more often as and when considered necessary by the Contracting States. Each Contracting State shall chair the SMC for a period of one year on rotational basis in alphabetical order.

Following are the instrument involved in SAFTA:-

- Trade Liberalisation Programme
- Rules of Origin
- Institutional Arrangements
- Consultations and Dispute Settlement Procedures
- Safeguard Measures
- Any other instrument that may be agreed upon.

Principles

The basic principles underlying SAFTA are as under;

1. overall reciprocity and mutuality of advantages so as to benefit equitably all Contracting States, taking into account their respective level of economic and industrial development, the pattern of their external trade, and trade and tariff policies and systems;
2. negotiation of tariff reform step by step, improved and extended in successive stages through periodic reviews;

3. recognition of the special needs of the Least Developed Contracting States and agreement on concrete preferential measures in their favour;
4. inclusion of all products, manufactures and commodities in their raw, semi-processed and processed forms.

Objectives of SAFTA

The objective of the agreement is to promote good competition in the free trade area and to provide equitable benefits to all the countries involved in the contracts. It aimed to benefit the people of the country by bringing transparency and integrity among the nations. SAFTA was also formed in order to increase the level of trade and economic cooperation among the SAARC nations by reducing the tariff and barriers and also to provide special preference to the Least Developed Countries (LDCs)among the SAARC nations. The basic objective of the agreement is to promote and enhance mutual trade and economic cooperation among member countries. Other objectives are as follows:-

- To eliminate barriers in trade and facilitate cross-border movement of goods between the territories of contracting states.
- To promote conditions of fair competition in the free trade area, and ensure equitable benefits to all contracting states, taking into account their respective levels and pattern of economic development.
- To create effective mechanism for the implementation and application of the agreement for its joint administration and the resolution of disputes.
- To establish a framework for further regional cooperation to expand and enhance the mutual benefits of the agreement.

Since the formation of SAARC in 1985 SAARC has accomplished, achieved and realized a number of goals and objectives. 17th SAARC Summit Declaration reaffirmed the commitment to peace, confidence building, liberty, human dignity, democracy, alleviation of poverty, reducing of inequality, mutual respect, and good governance, which would be crucial for economic and social development and for uplifting of standards of living of people of South Asia. “Four key agreements were signed during the last summit. These agreements were on Rapid response to Natural Disasters, establishment of a SAARC Seed Bank, SAARC Agreement on Recognition of Conformity Assessment and SAARC Agreement on Regional Standards respectively. All these Agreements, once implemented and executed, would enhance economic, commercial, trading and social dimension of the Region of SAARC. BUT SAFTA have not been able to do much due to enmity between the largest members, i.e., India and Pakistan.

Trade Liberalisation Programme

According to the Trade Liberalisation Programme Contracting countries must follow the following tariff reduction schedule. There should be a fall to 20% tariff from the existing tariff by the Non Least Developing Countries and 30% reduction from the existing tariff by the Least Developing Countries. But trade liberalisation scheme is not be applied for the sensitive list because this list is to be negotiated among the contracting countries and then to be traded. Sensitive list is a list with every country which does not include tariff concession. Sensitive list will involve common agreement among the contracting countries favouring the least developed contracting countries. SAFTA Ministerial Council (SMC) will be participating to review the sensitive list in every four years with view of reducing the list.

LESSON ROUND UP

- International trade and commerce is perhaps as old as civilization, the development of international economics as an independent branch of economic theory is a relatively recent phenomenon.
- International trade is the exchange of capital, goods, and services across international borders or territories. In most countries, such trade represents a significant share of gross domestic product (GDP).
- The first reasonably systematic body of thought devoted to international trade is called "mercantilism" and emerged in seventeenth and eighteenth century in Europe. The mercantilist writers argued that a key objective of trade should be to promote a favorable balance of trade.
- Adam Smith and the classical economists, claimed international trade was an efficient mechanism for allocating resources and for increasing national welfare, regardless of the level of a country's economic development.
- The theory of comparative advantage suggests that a country should export goods in the country in which its relative cost advantage, and not the absolute cost advantage, is greatest in comparison to other countries.
- The comparative advantage proposition states that a less developed country that lacks an absolute advantage in any goods can still engage in mutually beneficial trade, and that an advanced country whose domestic industries are more efficient than those in any other country can still benefit from trade even as some of its industries face intense import competition.
- A trade bloc is a type of intergovernmental agreement, often part of a regional intergovernmental organization, where regional barriers to trade, (tariffs and non-tariff barriers) are reduced or eliminated among the participating states.
- Depending on the level of economic integration, trade blocs can fall into six different categories, such as preferential trading areas, free trade areas, customs unions, common markets, economic union and monetary unions and political union .
- The objective of ASEAN is to accelerate the economic growth, social progress and cultural development in the region through joint endeavours in the spirit of equality and partnership in order to strengthen the foundation for a prosperous and peaceful community of South East Asian nations, and to promote regional peace and stability through abiding respect for Justice and the rule of law in the relationship among countries in the region and adherence to the principles of the United Nations Charter.
- The European Union (EU) has four main institutions namely, the Council of Ministers, the European Commission, the European Parliament and the European Court of Justice. Other bodies such as the Economic and Social Committee and the Committee of the Regions have particular roles to play in the decision making process.
- The South Asian Association for Regional Cooperation (SAARC) comprises Bangladesh, Bhutan, India, the Maldives, Nepal, Pakistan and Sri Lanka. The main goal of the Association is to accelerate the process of economic and social development in member states, through joint action in the agreed areas of cooperation.

SELF TEST QUESTIONS

1. What is international trade? Explain the reasons for international trade.
2. Explain absolute advantage theory of international trade. What limitations of absolute advantage led to development of comparative advantage theory of trade as given by Ricardo?

3. Write short notes on:
   (a) Mercantilism;
   (b) New trade theory
4. What is regional economic integration? Explain the six levels of economic integration.
5. Explain the advantages and disadvantage of regional trading blocs citing some real examples.
6. How did European Union emerge from European communities?
7. Why was SAFTA created and what objectives has it achieved?
8. Write short note on :
   (a) ASEAN
   (b) NAFTA

Lesson 7
Institutional Environment

LESSON OUTLINE

- World Trade Organisation
  - Principles of the trading system
  - History & Formation of WTO
  - Dispute Settlement Mechanism
  - Structure of WTO
  - The WTO Agreements
- UNCTAD
  - UNCTAD conferences
  - History of UNLTAD
  - Main goals & activities
  - Relationship with other agencies
- International Commodity Agreements
  - International Buffer Stock Agreements
  - International Export Quota Agreement
  - Some International Commodity Agreements
- World Bank
  - Functioning of the world bank
  - Contributions of the world bank
  - India and the world bank
- International Monetary Fund
  - Surveillance
  - Financial assistance
  - Technical assistance
  - India and the IMF
- Asia Development Bank
  - Policies and strategies
  - History
  - Working of ADB
  - India and ADB
- LESSON ROUND UP
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

Although international trade and investment are often described as occurring between countries, in practice, it is predominantly businesses, and increasingly consumers, that actually undertake trade and investment across borders, to take advantage of higher prices or profits for businesses, and lower prices or wider product choice for consumers. In addition, a country's domestic regulatory and policy settings and the implementation of its international commitments and regulations alter the country's economic conditions, and will affect its attractiveness as a source or destination of trade and investment.

Since 1947, trade barriers between nations have decreased dramatically. The Bretton Woods Conference of 1944 recognized the need for a comparable international institution for trade in addition to World Bank and International Monetary Fund. Multilateral trade institutions play a major role in promoting trade in the global environment. The individual countries lack direct enforcement power. The institutions can verify violations of the agreement and inform third parties. It can promote an efficient multilateral rule-making procedure. The enforcement and rule-making is particularly important when there are strong power imbalances in bilateral trading relationships.

This chapter provides an overview of various international institutions which facilitate and promote trade among the organisations in different countries. We will study about the rules, policies, how do these organisations work, their major contribution in the international trading environment.

"Free trade is a powerful instrument of freedom; a vibrant and dynamic market is the most powerful force for economic growth and sustainable development. This is not ideology talking. Facts speak for themselves and they tell us that free trade means bread, bread for the neediest of our people".

Colin Powell

WORLD TRADE ORGANIZATION

Overview

The World Trade Organization (WTO) deals with the rules of trade between nations at a global or near-global level. It's an organization for liberalizing trade. It's a forum for governments to negotiate trade agreements. It's a place for them to settle trade disputes. It operates a system of trade rules. Essentially, the WTO is a place where member governments go, to try to sort out the trade problems they face with each other.

The first step is to talk. The WTO was born out of negotiations, and everything the WTO does is the result of negotiations. The bulk of the WTO's current work comes from the 1986–94 negotiations called the Uruguay Round and earlier negotiations under the General Agreement on Tariffs and Trade (GATT). The WTO is currently the host to new negotiations, under the "Doha Development Agenda" launched in 2001.

WTO works through the WTO agreements which are negotiated and signed by the bulk of the world's trading nations. These documents provide the legal ground rules for international commerce. They are essentially contracts, binding governments to keep their trade policies within agreed limits. Although negotiated and signed by governments, the goal is to help producers of goods and services, exporters, and importers conduct their business, while allowing governments to meet social and environmental objectives.

The system's overriding purpose is to help trade flow as freely as possible so long as there are no undesirable side-effects because this is important for economic development and well-being. That partly means removing obstacles. It also means ensuring that individuals, companies and governments know what the trade rules are around the world, and giving them the confidence that there will be no sudden changes of policy. Lastly WTO also helps to settle disputes arising in the conduct of the business.

The system operated by the WTO is "Multilateral trading system", as almost all the main trading nations are members of the system but all countries of the world are not the members. So "multi-lateral" is used to describe the system instead of "global" or "world".

Few Facts:

1. *Location*: Geneva, Switzerland
2. *Established*: 1 January 1995
3. *Created by*: Uruguay Round negotiations (1986–94)
4. *Membership*: 153 countries (since 23 July 2008)
5. *Secretariat staff*: 625
6. *Head*: Pascal Lamy (Director-General)

Functions:

– Administering WTO trade agreements

– Forum for trade negotiations

– Handling trade disputes

– Monitoring national trade policies

– Technical assistance and training for developing countries

– Cooperation with other international organizations

PRINCIPLES OF THE TRADING SYSTEM

The WTO agreements are lengthy and complex because they are legal texts covering a wide range of activities. They deal with: agriculture, textiles and clothing, banking, telecommunications, government purchases, industrial standards and product safety, food sanitation regulations, intellectual property, and much more. But some fundamental principles run throughout all of these documents. These principles are the foundation of the multilateral trading system.

The principles:

The trading system should be ...

- without discrimination – a country should not discriminate between its trading partners (giving them equally "most-favored-nation" or MFN status); and it should not discriminate between its own and foreign products, services or nationals (giving them "national treatment");
- freer – barriers coming down through negotiation;
- predictable – foreign companies, investors and governments should be confident that trade barriers (including tariffs and non-tariff barriers) should not be raised arbitrarily; tariff rates and market-opening commitments are "bound" in the WTO;
- more competitive – discouraging "unfair" practices such as export subsidies and dumping products at below cost to gain market share;
- more beneficial for less developed countries – giving them more time to adjust, greater flexibility, and special privileges.

1. Trade without Discrimination

A. *Most-favoured-nation (MFN)*: "Treating other people equally". Under the WTO agreements, countries cannot normally discriminate between their trading partners. "If you grant someone a special favour (such as a lower customs duty rate for one of their products), you have to do the same for all other WTO members." This principle is known as most-favoured-nation (MFN) treatment. It is very important and the first article of the General Agreement on Tariffs and Trade (GATT), which governs trade in goods.

MFN is also a priority in the General Agreement on Trade in Services (GATS) (Article 2) and the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) (Article 4), although in each agreement the principle is handled slightly differently.

Some exceptions are allowed. For example –

- countries can set up a free trade agreement that applies only to goods traded within the group discriminating against goods from outside. Or
- they can give developing countries special access to their markets. Or
- a country can raise barriers against products that are considered to be traded unfairly from specific countries.
- And in services, countries are allowed, in limited circumstances, to discriminate.

But the agreements only permit these exceptions under strict conditions.

In general, MFN means that every time a country lowers a trade barrier or opens up a market, it has to do so for the same goods or ser-vices from all its trading partners – whether rich or poor, weak or strong.

Why 'most-favoured'?

It suggests special treatment, but in the WTO it actually means non-discrimination, treating virtually everyone equally. Each member treats all the other members equally as "most-favoured" trading partners. If a country improves the benefits that it gives to one trading partner, it has to give the same "best" treatment to all the other WTO members so that they all remain "most-favoured". The MFN principle ensures that each country treats its over-140 fellow-members equally.

B. *National treatment*: "Treating foreigners and locals equally". The principle of national treatment states that imported and locally-produced goods should be treated equally, at least after the foreign goods has entered the market. The same should apply to foreign and domestic services, and to foreign and local trademarks, copyrights and patents. This principle of "national treatment" (giving others the same treatment as one's own nationals) is also found in all the three main WTO agreements (Article 3 of GATT, Article 17 of GATS and Article 3 of TRIPS), although once again the principle is handled slightly differently in each of these. National treatment only applies once a product, service or item of intellectual property has entered the market. Therefore, charging customs duty on an import is not a violation of national treatment even if locally-produced products are not charged an equivalent tax.

2. Freer Trade: Gradually through Negotiation

Lowering trade barriers is one of the most obvious means of encouraging trade. The barriers concerned include customs duties (or tariffs) and measures such as import bans or quotas that restrict quantities selectively. From time to time other issues such as red tape and exchange rate policies have also been discussed.

Since GATT's creation in 1947–48 there have been eight rounds of trade negotiations. A ninth round, under the Doha Development Agenda, is now underway. At first these focused on lowering tariffs (customs duties) on imported goods. As a result of the negotiations, by the mid-1990s industrial countries' tariff rates on industrial goods had fallen steadily to less than 4%.

But by the 1980s, the negotiations had expanded to cover non-tariff barriers on goods, and to the new areas such as services and intellectual property.

Opening markets can be beneficial, but it also requires adjustment. The WTO agreements allow countries to introduce changes gradually, through "progressive liberalization". Developing countries are usually given longer to fulfill their obligations.

3. Predictability: Through Binding and Transparency

Sometimes, promising not to raise a trade barrier can be as important as lowering one, because the promise gives businesses a clearer view of their future opportunities. With stability and predictability, investment is encouraged, jobs are created and consumers can fully enjoy the benefits of competition choice and lower prices. The multilateral trading system is an attempt by governments to make the business environment stable and predictable.

In the WTO, when countries agree to open their markets for goods or services, they "bind" their commitments. For goods, these bindings amount to ceilings on customs tariff rates. Sometimes countries tax imports at rates that are lower than the bound rates. Frequently this is the case in developing countries. In developed countries the rates actually charged and the bound rates tend to be the same.

A country can change its bindings, but only after negotiating with its trading partners, which could mean compensating them for loss of trade. In agriculture, 100% of products now have bound tariffs. The result of all this: a substantially higher degree of market security for traders and investors.

The system tries to improve predictability and stability in other ways as well. One way is to discourage the use of quotas and other measures used to set limits on quantities of imports. Administering quotas can lead to more red-tape and accusations of unfair play. Another is to make countries' trade rules as clear and public ("transparent") as possible. Many WTO agreements require governments to disclose their policies and practices publicly within the country or by

notifying the WTO. The regular surveillance of national trade policies through the Trade Policy Review Mechanism provides a further means of encouraging transparency both domestically and at the multilateral level.

4. Promoting Fair Competition

The WTO is sometimes described as a "free trade" institution, but that is not entirely accurate. The system does allow tariffs and, in limited circumstances, other forms of protection. More accurately, it is a system of rules dedicated to open, fair and undistorted competition.

The rules on non-discrimination MFN, national treatment dumping and subsidies etc. are designed to secure fair conditions of trade. The rules try to establish what is fair or unfair, and how governments can respond, in particular by charging additional import duties calculated to compensate for damage caused by unfair trade.

Many of the other WTO agreements aim to support fair competition: in agriculture, intellectual property, services etc. The agreement on government procurement (a "plurilateral" agreement because it is signed by only a few WTO members) extends competition rules to purchases by thousands of government entities in many countries.

5. Encouraging Development and Economic Reform

The WTO system contributes to development. The agreements themselves inherit the provisions of GATT that allow for special assistance and trade concessions for developing countries. Over three quarters of WTO members are developing countries and countries in transition to market economies.

During the seven and a half years of the Uruguay Round, over 60 of these countries implemented trade liberalization programmes autonomously. At the same time, developing countries and transition economies were much more active and influential in the Uruguay Round negotiations than in any previous round, and they are even more so in the current Doha Development Agenda.

At the end of the Uruguay Round, developing countries were prepared to take on most of the obligations that are required of developed countries. But the agreements did give them transition periods to adjust to the more unfamiliar and difficult WTO provisions, particularly so for the poorest, "least-developed" countries.

A ministerial decision adopted at the end of the Uruguay round says better-off countries should accelerate implementing market access commitments on goods exported by the least-developed countries, and seeks increased technical assistance for them. More recently, developed countries have started to allow duty-free and quota-free imports for almost all products from least-developed countries.

The current Doha Development Agenda includes developing countries' concerns about the difficulties they face in implementing the Uruguay Round agreements.

HISTORY AND FORMATION OF WTO

The WTO's creation on 1 January 1995 marked the biggest reform of international trade since after the Second World War. It also brought to reality, in an updated form, the failed attempt in 1948 to create an International Trade Organization.

Much of the history of those 47 years was written in Geneva. But it also traces a journey that spanned the continents, from that hesitant start in 1948 in Havana (Cuba), via Annecy (France), Torquay (UK), Tokyo (Japan), Punta del Este (Uruguay), Montreal (Canada), Brussels (Belgium) and finally to Marrakesh (Morocco) in 1994. During that period, the trading system came under GATT, salvaged from the aborted attempt to create the ITO. GATT helped establish a strong and prosperous multilateral trading system that became more and more liberal through rounds of trade negotiations. But by the 1980s the system needed a thorough overhaul. This led to the Uruguay Round, and ultimately to the WTO.

GATT: 'provisional' for almost half a century

From 1948 to 1994, the General Agreement on Tariffs and Trade (GATT) provided the rules for much of world

trade and presided over periods that saw some of the highest growth rates in international commerce. It seemed well-established, but throughout those 47 years, it was a provisional agreement and organization.

The original intention was to create a third institution to handle the trade side of inter-national economic cooperation, joining the two "Bretton Woods" institutions, the World Bank and the International Monetary Fund. Over 50 countries participated in negotiations to create an International Trade Organization (ITO) as a specialized agency of the United Nations. The draft ITO Charter was ambitious. It extended beyond world trade disciplines, to include rules on employment, commodity agreements, restrictive business practices, international investment, and services. The aim was to create the ITO at a UN Conference on Trade and Employment in Havana, Cuba in 1947.

Meanwhile, 15 countries had begun talks in December 1945 to reduce and bind customs tariffs. With the Second World War only recently ended, they wanted to give an early boost to trade liberalization, and to begin to correct the legacy of protectionist measures which remained in place from the early 1930s.

This first round of negotiations resulted in a package of trade rules and 45,000 tariff concessions affecting $10 billion of trade, about one fifth of the world's total. The group had expanded to 23 by the time the deal was signed on 30 October 1947. The tariff concessions came into effect by 30 June 1948 through a "Protocol of Provisional Application". And so the new General Agreement on Tariffs and Trade was born, with 23 founding members (officially "contracting parties").

The 23 were also part of the larger group negotiating the ITO Charter. One of the provisions of GATT says that they should accept some of the trade rules of the draft. This, they believed, should be done swiftly and "provisionally" in order to protect the value of the tariff concessions they had negotiated. They spelt out how they envisaged the relationship between GATT and the ITO Charter, but they also allowed for the possibility that the ITO might not be created. They were right.

The Havana conference began on 21 November 1947, less than a month after GATT was signed. The ITO Charter was finally agreed in Havana in March 1948, but ratification in some national legislatures proved impossible. The most serious opposition was in the US Congress, even though the US government had been one of the driving forces. In 1950, the United States government announced that it would not seek Congressional ratification of the Havana Charter, and the ITO was effectively dead. So, the GATT became the only multilateral instrument governing international trade from 1948 until the WTO was established in 1995.

For almost half a century, the GATT's basic legal principles remained much as they were in 1948. There were additions in the form of a section on development added in the 1960s and "plurilateral" agreements (i.e. with voluntary membership) in the 1970s, and efforts to reduce tariffs further continued. Much of this was achieved through a series of multilateral negotiations known as "trade rounds" – the biggest leaps forward in international trade liberalization have come through these rounds which were held under GATT's auspices.

In the early years, the GATT trade rounds concentrated on further reducing tariffs. Then, the Kennedy Round in the mid-sixties brought about a GATT Anti-Dumping Agreement and a section on development. The Tokyo Round during the seventies was the first major attempt to tackle trade barriers that do not take the form of tariffs, and to improve the system. The eighth, the Uruguay Round of 1986–94, was the last and most extensive of all. It led to the WTO and a new set of agreements.

They were not multilateral, but they were a beginning. Several codes were eventually amended in the Uruguay Round and turned into multilateral commitments accepted by all WTO members. Only four remained "plurilateral" – those on government procurement, bovine meat, civil aircraft and dairy products. In 1997 WTO members agreed to terminate the bovine meat and dairy agreements, leaving only two.

The Tokyo Round: A First Try to Reform the System

The Tokyo Round lasted from 1973 to 1979, with 102 countries participating. It continued GATT's efforts to progressively reduce tariffs. The results included an average one-third cut in customs duties in the world's nine major industrial markets, bringing the average tariff on industrial products down to 4.7%. The tariff reductions, phased in over a period of eight years, involved an element of "harmonization"– the higher the tariff, the larger the cut, proportionally. In other issues, the Tokyo Round had mixed results. It failed to come to grips with the

fundamental problems affecting farm trade and also stopped short of providing a modified agreement on "safeguards" (emergency import measures). Nevertheless, a series of agreements on non-tariff barriers did emerge from the negotiations, in some cases interpreting existing GATT rules, in others breaking entirely new ground. In most cases, only a relatively small number of (mainly industrialized) GATT members subscribed to these agreements and arrangements. Because they were not accepted by the full GATT membership, they were often informally called "codes".

They were not multilateral, but they were a beginning. Several codes were eventually amended in the Uruguay Round and turned into multilateral commitments accepted by all WTO members. Only four remained "plurilateral" – those on government procurement, bovine meat, civil aircraft and dairy products. In 1997 WTO members agreed to terminate the bovine meat and dairy agreements, leaving only two.

Did GATT succeed?

GATT was provisional with a limited field of action, but its success over 47 years in promoting and securing the liberalization of much of world trade is incontestable. Continual reductions in tariffs alone helped spur very high rates of world trade growth during the 1950s and 1960s – around 8% a year on average. And the momentum of trade liberalization helped ensure that trade growth consistently out-paced production growth throughout the GATT era, a measure of countries' increasing ability to trade with each other and to reap the benefits of trade. The rush of new members during the Uruguay Round demonstrated that the multilateral trading system was recognized as an anchor for development and an instrument of economic and trade reform.

But all was not well. As time passed new problems arose. The Tokyo Round in the 1970s was an attempt to tackle some of these but its achievements were limited. This was a sign of difficult times to come.

GATT's success in reducing tariffs to such a low level, combined with a series of economic recessions in the 1970s and early 1980s, drove governments to devise other forms of protection for sectors facing increased foreign competition. High rates of unemployment and constant factory closures led governments in Western Europe and North America to seek bilateral market-sharing arrangements with competitors and to embark on a subsidies race to maintain their holds on agricultural trade. Both these changes undermined GATT's credibility and effectiveness.

The problem was not just a deteriorating trade policy environment. By the early 1980s the General Agreement was clearly no longer as relevant to the realities of world trade as it had been in the 1940s. For a start, world trade had become far more complex and important than 40 years before: the globalization of the world economy was underway, trade in services – not covered by GATT rules – was of major interest to more and more countries, and international investment had expanded. The expansion of services trade was also closely tied to further increases in world merchandise trade. In other respects, GATT had been found wanting. For instance, in agriculture, loopholes in the multilateral system were heavily exploited, and efforts at liberalizing agricultural trade met with little success. In the textiles and clothing sector, an exception to GATT's normal disciplines was negotiated in the 1960s and early 1970s, leading to the Multifibre Arrangement. Even GATT's institutional structure and its dispute settlement system were causing concern.

These and other factors convinced GATT members that a new effort to reinforce and extend the multilateral system should be attempted. That effort resulted in the Uruguay Round, the Marrakesh Declaration, and the creation of the WTO.

The Uruguay Round

It took seven and a half years, almost twice the original schedule. By the end, 123 countries were taking part. It covered almost all trade, from toothbrushes to plea-sure boats, from banking to telecommunications, from the genes of wild rice to AIDS treatments. It was quite simply the largest trade negotiation ever, and most probably the largest negotiation of any kind in history.

At times it seemed doomed to fail. But in the end, the Uruguay Round brought about the biggest reform of the world's trading system since GATT was created at the end of the Second World War. And yet, despite its troubled progress, the Uruguay Round did see some early results. Within only two years, participants had agreed on a package of cuts in import duties on tropical products – which are mainly exported by developing countries. They had also revised the rules for settling disputes, with some measures implemented on the spot.

And they called for regular reports on GATT members' trade policies, a move considered important for making trade regimes transparent around the world.

A round to end all rounds?

The seeds of the Uruguay Round were sown in November 1982 at a ministerial meeting of GATT members in Geneva. Although the ministers intended to launch a major new negotiation, the conference stalled on agriculture and was widely regarded as a failure. In fact, the work programme that the ministers agreed formed the basis for what was to become the Uruguay Round negotiating agenda.

Nevertheless, it took four more years of exploring, clarifying issues and painstaking consensus-building, before ministers agreed to launch the new round. They did so in September 1986, in Punta del Este, Uruguay. They eventually accepted a negotiating agenda that covered virtually every outstanding trade policy issue. The talks were going to extend the trading system into several new areas, notably trade in services and intellectual property, and to reform trade in the sensitive sectors of agri-culture and textiles. All the original GATT articles were up for review. It was the biggest negotiating mandate on trade ever agreed, and the ministers gave themselves four years to complete it.

Two years later, in December 1988, ministers met again in Montreal, Canada, for what was supposed to be an assessment of progress at the round's half-way point. The purpose was to clarify the agenda for the remaining two years, but the talks ended in a deadlock that was not resolved until officials met more quietly in Geneva the following April.

Despite the difficulty, during the Montreal meeting, ministers did agree a package of early results. These included some concessions on market access for tropical products – aimed at assisting developing countries – as well as a streamlined dispute settlement system, and the Trade Policy Review Mechanism which provided for the first comprehensive, systematic and regular reviews of national trade policies and practices of GATT members. The round was supposed to end when ministers met once more in Brussels, in December 1990. But they disagreed on how to reform agricultural trade and decided to extend the talks. The Uruguay Round entered its bleakest period.

Despite the poor political outlook, a considerable amount of technical work continued, leading to the first draft of a final legal agreement. This draft "Final Act" was compiled by the then GATT director-general, Arthur Dunkel, who chaired the negotiations at officials' level. It was put on the table in Geneva in December 1991. The text fulfilled every part of the Punta del Este mandate, with one exception – it did not contain the participating countries' lists of commitments for cutting import duties and opening their services markets. The draft became the basis for the final agreement.

Over the following two years, the negotiations lurched between impending failure, to predictions of imminent success. Several deadlines came and went. New points of major conflict emerged to join agriculture: services, market access, anti-dumping rules, and the proposed creation of a new institution. Differences between the United States and European Union became central to hopes for a final, successful conclusion.

In November 1992, the US and EU settled most of their differences on agriculture in a deal known informally as the "Blair House accord". By July 1993 the "Quad" (US, EU, Japan and Canada) announced significant progress in negotiations on tariffs and related subjects ("market access"). It took until 15 December 1993 for every issue to be finally resolved and for negotiations on market access for goods and ser-vices to be concluded (although some final touches were completed in talks on mar-ket access a few weeks later). On 15 April 1994, the deal was signed by ministers from most of the 123 participating governments at a meeting in Marrakesh, Morocco.

The delay had some merits. It allowed some negotiations to progress further than would have been possible in 1990: for example some aspects of services and intellectual property, and the creation of the WTO itself. But the task had been immense, and negotiation-fatigue was felt in trade bureaucracies around the world. The difficulty of reaching agreement on a complete package containing almost the entire range of current trade issues led some to conclude that a negotiation on this scale would never again be possible. Yet, the Uruguay Round agreements contain time-tables for new negotiations on a number of topics. And by 1996, some countries were openly calling for a new round early in the next century. The response was mixed; but the Marrakesh agreement did already include commitments to reopen negotiations on agriculture and services at the turn of the century. These began in early 2000 and were incorporated into the Doha Development Agenda in late 2001.

What happened to GATT?

The WTO replaced GATT as an international organization, but the General Agreement still exists as the WTO's umbrella treaty for trade in goods, updated as a result of the Uruguay Round negotiations.

The post-Uruguay Round built-in agenda

There were over 30 items in the original built-in agenda. The agenda originally built into the Uruguay Round agreements has seen additions and modifications. Some negotiations were quickly completed, notably in basic telecommunications, financial services. A number of other items are now part of the Doha Agenda, some of them updated. Some of the main highlights of agenda are presented below :

1996	– Maritime services: market access negotiations to end (30 June 1996, suspended to 2000, now part of Doha Development Agenda) – Services and environment: deadline for working party report (ministerial conference, December 1996) – Government procurement of services: negotiations start
1997	– Basic telecoms: negotiations end (15 February) – Financial services: negotiations end (30 December) – Intellectual property, creating a multilateral system of notification and registration of geographical indications for wines: negotiations start, now part of Doha Development Agenda
1998	– Textiles and clothing: new phase begins 1 January – Services (emergency safeguards): results of negotiations on emergency safeguards to take effect (by 1 January 1998, deadline now March 2004) – Rules of origin: Work programme on harmonization of rules of origin to be completed (20 July 1998) – Government procurement: further negotiations start, for improving rules and procedures (by end of 1998) – Dispute settlement: full review of rules and procedures (to start by end of 1998)
1999	– Intellectual property: certain exceptions to patentability and protection of plant varieties: review starts
2000	– Agriculture: negotiations start, now part of Doha Development Agenda – Services: new round of negotiations start, now part of Doha Development Agenda – Tariff bindings: review of definition of "principle supplier" having negotiating rights under GATT Art 28 on modifying bindings – Intellectual property: first of two-yearly reviews of the implementation of the agreement

2002	– Textiles and clothing: new phase begins 1 January
2005	– Textiles and clothing: full integration into GATT and agreement expires 1 January

HOW IS THE WTO DIFFERENT FROM GATT?

The World Trade Organization is not a simple extension of GATT, rather it completely replaces its predecessor and has a very different character. The principal differences are given below:

GATT	WTO
The GATT was a set of rules, a multilateral agreement, with no institutional foundation, only a small associated secretariat which had its origins in the attempt to establish an International Trade Organization in the 1940s.	The WTO is a permanent institution with its own secretariat.
The GATT was applied on a "provisional basis" even if, after more than forty seven years, governments chose to treat it as a permanent commitment.	The WTO commitments are full and permanent.
The GATT rules applied to trade in merchandise goods.	In addition to goods, the WTO covers trade in services and trade-related aspects of intellectual property.
While GATT was a multilateral instrument, by the 1980s many new agreements had been added of a plurilateral, and therefore selective in nature.	The agreements which constitute the WTO are almost all multilateral and, thus, involve commitments for the entire membership.
GATT 1947 was an institution as well as an agreement.	WTO has replaced GATT 1947 as an institution, whereas GATT 1994 is GATT 1947 as amended until the Uruguay Round of Negotiations.
The dispute settlement system was not faster, automatic and susceptible to blockages.	The WTO dispute settlement system is faster, more automatic, and thus much less susceptible to blockages, than the old GATT system. The implementation of WTO dispute findings will also be more easily assured.
GATT has contracting Parties, underscoring the fact that officially GATT was a legal text.	The WTO has members.

DISPUTE SETTLEMENT MECHANISM

Dispute settlement is the central pillar of the multilateral trading system. Without a means of settling disputes, the rules-based system would be less effective because the rules could not be enforced. The system is based on clearly-defined rules, with timetables for completing a case.

- First rulings are made by a panel and endorsed (or rejected) by the WTO's full membership.
- Appeals based on points of law are possible.

However, the point is not to pass judgement. The priority is to settle disputes, through consultations if possible. By January 2008, only about 136 of the 369 cases had reached the full panel process. Most of the rest have either been notified as settled "out of court" or remain in a prolonged consultation phase since 1995.

Principles of Dispute Settlement

A dispute arises when one country adopts a trade policy measure or takes some action that one or more fellow-WTO members considers to be breaking the WTO agreements, or to be a failure to live up to obligations. A third group of countries can declare that they have an interest in the case and enjoy some rights. Disputes in the WTO are essentially about broken promises. WTO members have agreed that if they believe fellow-members are violating trade rules, they will use the multilateral system of settling disputes instead of taking action unilaterally. That means abiding by the agreed procedures, and respecting judgements. The dispute settlement procedure is based on the following principles –

- equitable,
- fast,
- effective,
- mutually acceptable

Comparison of Dispute Settlement Under GATT and Uruguay Round

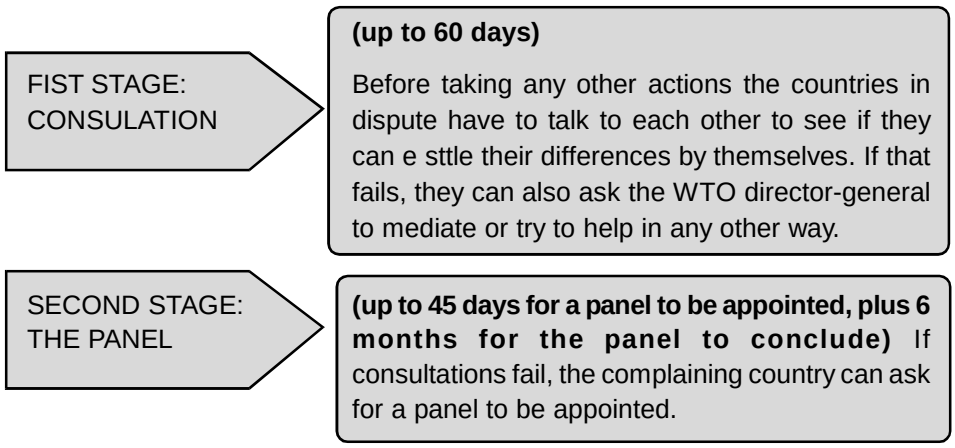
A procedure for settling disputes existed under the old GATT, but it had no fixed timetables, rulings were easier to block, and many cases dragged on for a long time inconclusively. The Uruguay Round agreement introduced a more structured process with more clearly defined stages in the procedure. It introduced greater discipline for the length of time a case should take to be settled, with flexible deadlines set in various stages of the procedure. The agreement emphasizes that prompt settlement is essential if the WTO is to function effectively. It sets out in considerable detail the procedures and the timetable to be followed in resolving disputes. If a case runs its full course to a first ruling, it should not normally take more than about one year to 15 months if the case is appealed. The agreed time limits are flexible, and if the case is considered urgent (e.g. if perishable goods are involved), it is accelerated as much as possible.

The Uruguay Round agreement also made it impossible for the country losing a case to block the adoption of the ruling. Under the previous GATT procedure, rulings could only be adopted by consensus, meaning that a single objection could block the ruling. Now, rulings are automatically adopted unless there is a consensus to reject a ruling. Any country wanting to block a ruling has to persuade all other WTO members (including its adversary in the case) to share its view.

Although much of the procedure does resemble a court or tribunal, the preferred solution is for the countries concerned to discuss their problems and settle the dispute by themselves. The first stage is therefore consultations between the governments concerned, and even when the case has progressed to other stages, consultation and mediation are still always possible.

How are disputes settled?

Settling disputes is the responsibility of the Dispute Settlement Body (the General Council), which consists of all WTO members. The Dispute Settlement Body has the sole authority to establish "panels" of experts to consider the case, and to accept or reject the panels' findings or the results of an appeal. It monitors the implementation of the rulings and recommendations, and has the power to authorize retaliation when a country does not comply with a ruling.



The Panel Process

Appointment of Panel: The panellists are usually chosen in consultation with the countries in dispute. Only if the two sides cannot agree does the WTO director-general appoint them. The country "in the dock" can block the creation of a panel once, but when the Dispute Settlement Body meets for a second time, the appointment can no longer be blocked (unless there is a consensus against appointing the panel).

Panels consist of three to five experts from different countries who examine the evidence and decide who is right and who is wrong. Panellists for each case can be chosen from a permanent list of well-qualified candidates, or from elsewhere. They serve in their individual capacities. They cannot receive instructions from any government.

Power of Panel: Officially, the panel is helping the Dispute Settlement Body make rulings or recommendations. The panel's report is passed to the Dispute Settlement Body, which can only reject the report by consensus. Since, the panel's report can only be rejected by consensus in the Dispute Settlement Body, its conclusions are difficult to overturn. The panel's findings have to be based on the agreements cited.

Working of a Panel: A dispute can go through the various stages in the WTO. At all stages, countries in dispute are encouraged to consult each other in order to settle "out of court". At all stages, the WTO director-general is available to offer his good offices, to mediate or to help achieve a conciliation. The main stages of how the panel works are given below.

1. ***Before the first hearing*****:** Each side in the dispute presents its case in writing to the panel.
2. ***First hearing*****:** the case for the complaining country and defence: the complaining country (or countries), the responding country, and those that have announced they have an interest in the dispute, make their case at the panel's first hearing.
3. ***Rebuttals*****:** the countries involved submit written rebuttals and present oral arguments at the panel's second meeting.
4. ***Experts*****:** if one side raises scientific or other technical matters, the panel may consult experts or appoint an expert review group to prepare an advisory report.
5. ***First draft*****:** the panel submits the descriptive (factual and argument) sections of its report to the two sides, giving them two weeks to comment. This report does not include findings and conclusions.
6. ***Interim report*****:** The panel then submits an interim report, including its findings and conclusions, to the two sides, giving them one week to ask for a review.
7. ***Review*****:** The period of review must not exceed two weeks. During that time, the panel may hold additional meetings with the two sides.
8. ***Final report*****:** The panel's final report should normally be given to the parties to the dispute with-in six months. In cases of urgency, including those concerning perishable goods, the deadline is shortened to

three months. A final report is submitted to the two sides and three weeks later, it is circulated to all WTO members. If the panel decides that the disputed trade measure does break a WTO agreement or an obligation, it recommends that the measure be made to conform with WTO rules. The panel may suggest how this could be done.

9. ***The report becomes a ruling*:** The report becomes the Dispute Settlement Body's ruling or recommendation within 60 days unless a consensus rejects it. Both sides can appeal the report (and in some cases both sides do).
10. ***Appeals*:** Either side can appeal a panel's ruling. Sometimes both sides do so. Appeals have to be based on points of law such as legal interpretation – they cannot reexamine existing evidence or examine new issues.

Each appeal is heard by three members of a permanent seven-member Appellate Body set up by the Dispute Settlement Body and broadly representing the range of WTO membership. Members of the Appellate Body have four-year terms. They have to be individuals with recognized standing in the field of law and international trade, not affiliated with any government.

The appeal can uphold, modify or reverse the panel's legal findings and conclusions. Normally appeals should not last more than 60 days, with an absolute maximum of 90 days.

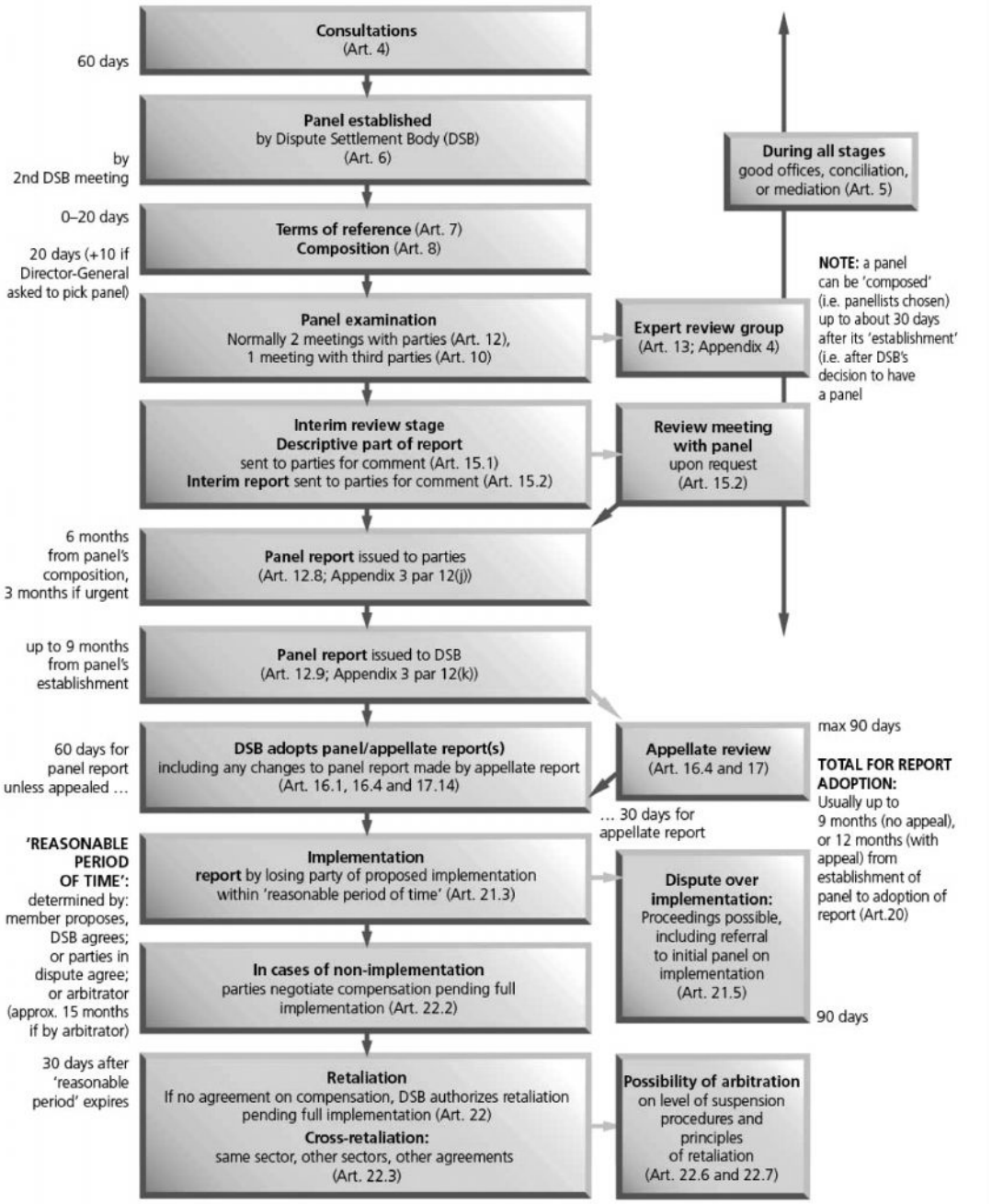
The Dispute Settlement Body has to accept or reject the appeals report within 30 days and rejection is only possible by consensus

How long to settle a dispute?

These approximate periods for each stage of a dispute settlement procedure are target figures — the agreement is flexible. In addition, the countries can settle their dispute themselves at any stage. Totals are also approximate,

60 days	Consultations, mediation, etc
45 days	Panel set up and panellists appointed
6 months	Final panel report to parties
3 weeks	Final panel report to WTO members
60 days	Dispute Settlement Body adopts report (if no appeal)
Total = 1 year	(without appeal)
60-90 days 30 days	Appeals report Dispute Settlement Body adopts appeals report
Total = 1y 3m	(with appeal)

DIAGRAMATIC REPRESENTATION OF THE PANEL PROCESS



Case Study - Dispute Settlement System of the WTO

Introduction

The WTO is playing a novel role in promoting trade relations. Access to a multilateral dispute settlement system is helping to scrutinize the regional disciplines. Although participation in WTO dispute settlement is too costly and time consuming, the WTO provides the intangible benefit of exposure to all the parties involved.

In March 2007, the United States requested consultations with India with respect to “additional duties” or “extra additional duties” that India applies to imports from the United States. The United States had challenged two types of duties imposed by India on imports of certain products entering its customs territory. The Dispute Settlement panel of WTO was formed to consider a complaint by the United States concerning two specific

duties – the "Additional Duty" imposed by India at the border on imports of alcoholic liquor for human consumption (beer, wine, and distilled spirits, collectively "alcoholic beverages"); and the "Extra-Additional Duty" imposed by India at the border on imports of a wider range of products, including certain agricultural and industrial products, as well as alcoholic beverages entering its customs territory.

The United States claims that the measures are inconsistent with Articles II:1(a) and (b), and III:2 and III:4 of the GATT 1994. The United States claimed before the Panel, that the Additional Duty, when imposed in conjunction with the Basic Customs Duty, is inconsistent with India's obligations under Articles II:1(a) and II:1(b) of the GATT 1994 because it results in the imposition of ordinary customs duties ("OCDs") or other duties or charges ("ODCs") that exceed the bound rates set out in India's Schedule of Concessions. The United States brought a similar claim against the Extra-Additional Duty.

India argued that it collects these duties in addition to its basic customs duty imposed under Section 12 of India's Customs Act of 1962 (the "Basic Customs Duty") . According to India, the Additional Duty and the Extra-Additional Duty are taken to counter-balance various internal taxes or charge. India argued that the measures challenged by the United States are charges on the importation of products that are equivalent to internal taxes imposed in respect of like domestic products. As such, India argued that they are subject to Article II:2(a) and do not fall within the scope of Article II:1(b) .

On 16 March 2007, the European Communities requested to join the consultations. On 21 March 2007, Australia requested to join the consultations. Subsequently, India informed the DSB that it had accepted the request of the European Communities to join the consultations. On 24 May 2007, the United States requested the establishment of a panel. At its meeting on 4 June 2007, the DSB deferred the establishment of a panel.

Panel and Appellate Body proceedings

At its meeting on 20 June 2007, the DSB established a panel. Australia, Chile, the European Communities, Japan and Viet Nam reserved their third-party rights. On 3 July 2007, the panel was composed. On 17 December 2007, the Chairman of the Panel informed the DSB that due to the complexity of the dispute, and the administrative and procedural matters involved, the Panel is not able to complete its work in six months. The Panel expects to issue its final report to the parties in the course of March 2008.

The Panel report was circulated to Members on 9 June 2008. The Panel concluded that the United States has failed to establish that the Additional Duty on alcoholic liquor is inconsistent with Article II:1(a) or (b) of the GATT 1994 and that it has also failed to establish that the SUAD is inconsistent with Article II:1(a) or (b) of the GATT 1994.

In the light of these conclusions, the Panel made no recommendations under Article 19.1 of the DSU. However, it offered some concluding remarks. The panel recalled that, after the establishment of this Panel, India issued new customs notifications making certain changes to the AD on alcoholic liquor and the SUAD, "to address concerns raised by [India's] trading partners". The Panel noted that, therefore, its disposition of the US claims under Article II:1(a) and (b) does not necessarily imply that it would be consistent with India's WTO obligations for India to withdraw the relevant new customs notifications or otherwise re-establish the status quo ante, i.e., the situation as it existed on the date of establishment of the Panel. By the same token, in making this point, the panel did not wish to suggest that the entry into force of the new customs notifications necessarily implies that the AD on alcoholic liquor, to the extent it still exists, and the SUAD are WTO-consistent.

On 1 August 2008, the United States notified its decision to appeal to the Appellate Body certain issues of law covered in the Panel report and certain legal interpretations developed by the Panel. On 13 August 2008, India notified its decision to appeal to the Appellate Body certain issues of law and legal interpretations developed by the Panel. On 25 September 2008, the Chairman of the Appellate Body informed the DSB that due to the time required for completion and translation of the report, the Appellate Body would not be able to circulate its report within 60 days. The Appellate Body report would be circulated no later than 30 October 2008.

On 30 October 2008, the Appellate Body report was circulated to Members. The Appellate Body found:

The Appellate Body rejected the United States' claim that the Panel limited the scope of the United States'

challenge to the Additional Duty as imposed only through Customs Notification 32/2003, and the Extra-Additional Duty as imposed only through Customs Notification 19/2006.

As regards the Panel's findings with respect to the interpretation of Articles II:1(b) and II:2(a), the Appellate Body found that the Panel erred in its interpretation that Article II:1(b) covers only duties or charges that "inherently discriminate against imports", that the Panel erred in interpreting the term "equivalent" in Article II:2(a) as requiring only a qualitative comparison of the relative function of a charge and internal tax, thereby incorrectly excluding quantitative considerations relating to their effect and amount, and that the Panel also erred in finding that "consistency with Article III:2" is not a necessary condition in the application of Article II:2(a). Consequently, the Appellate Body reversed the Panel's findings that the United States failed to establish that the Additional Duty and the Extra-Additional Duty are inconsistent with Articles II:1(a) and II:1(b) of the GATT 1994.

The Appellate Body also found that the United States was required to present arguments and evidence that the Additional Duty and the Extra-Additional Duty are not justified under Article II:2(a), and that India, in asserting that those duties are justified, was required to adduce arguments and evidence in support of its assertion.

The Appellate Body also considered that the Additional Duty would not be justified under Article II:2(a) of the GATT 1994 in so far as it results in the imposition of charges on imports of alcoholic beverages in excess of the excise duties applied on like domestic products, and, consequently, that this would render the Additional Duty inconsistent with Article II:1(b) to the extent that it results in the imposition of duties in excess of those set forth in India's Schedule of Concessions.

The Appellate Body also considered that the Extra-Additional Duty would not be justified under Article II:2(a) of the GATT 1994 insofar as it results in the imposition of charges on imports in excess of the sales taxes, value-added taxes, and other local taxes or charges that India alleges are equivalent to the Extra-Additional Duty; and, consequently, that this would render the Extra-Additional Duty inconsistent with Article II:1(b) to the extent that it results in the imposition of duties in excess of those set forth in India's Schedule of Concessions.

Finally, the Appellate Body found that the Panel did not act contrary to Articles 3.2, 11, and 19 of the DSU in providing "concluding remarks" in paragraph 8.2 of the Panel Report. In view of its findings and conclusions, the Appellate Body made no recommendation, in this case, to the Dispute Settlement Body pursuant to Article 19.1 of the DSU.

At its meeting on 17 November 2008, the DSB adopted the Appellate Body report and the Panel report, as reversed by the Appellate Body report.

In view of the facts and circumstances given in the case above, comment on the dispute settlement procedure of WTO on the basis of the given case. Has India benefitted by becoming a member of WTO? Critically examine.

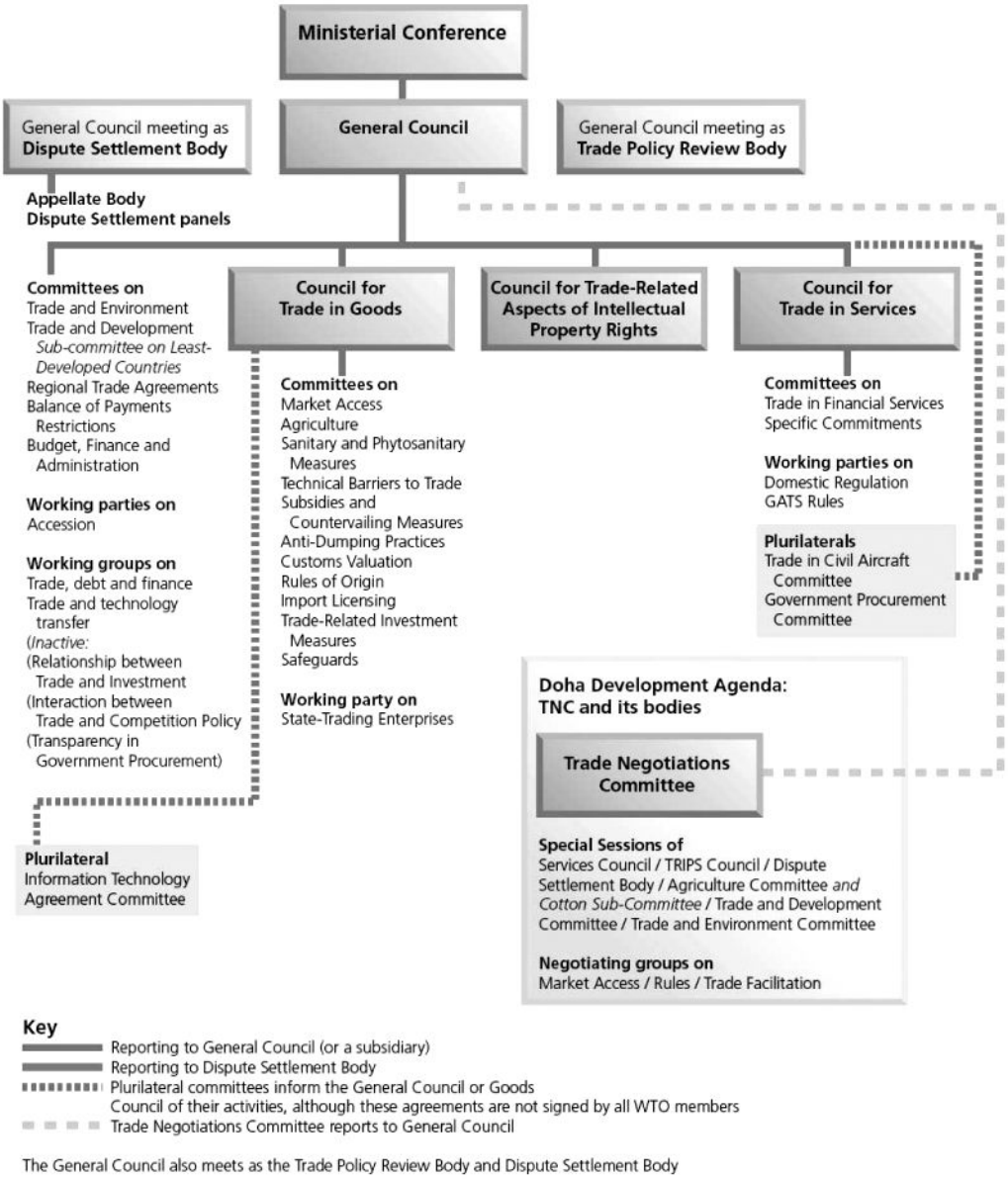
WTO STRUCTURE

The WTO has 153 members, accounting for over 97% of world trade. Around 30 others are negotiating membership. Decisions are made by the entire membership. This is typically by consensus. A majority vote is also possible but it has never been used in the WTO, and was extremely rare under the WTO's predecessor, the General Agreement on Tariffs and Trade (GATT). The WTO's agreements have been ratified in all members' parliaments. The WTO's top level decision-making body is the Ministerial Conference which meets at least once every two years.

Below this is the General Council (normally ambassadors and heads of delegation in Geneva, but sometimes officials sent from members' capitals) which meets several times a year in the Geneva headquarters. The General Council also meets as the Trade Policy Review Body and the Dispute Settlement Body. At the next level, the Goods Council, Services Council and the Intellectual Property (TRIPS) Council report to the General Council.

Numerous specialized committees and working groups and working parties deal with the individual agreements and other areas such as the environment, development, membership applications and regional trade agreements.

All WTO members may participate in all councils, committees, etc, except Appellate Body, Dispute Settlement panels, Textiles Monitoring Body, and plurilateral committees.



The General Council also meets as the Trade Policy Review Body and Dispute Settlement Body

WTO SECRETARIAT

The WTO Secretariat, based in Geneva, has around 625 staff and is headed by a director general. It does not have branch offices outside Geneva. Since decisions are taken by the Members themselves, the Secretariat does not have the decision-making role that other international bureaucracies are given. The Secretariat's main duties are to supply technical support for the various councils and committees and the ministerial conferences, to provide technical assistance for developing countries, to analyze world trade, and to explain WTO affairs to the public and media. The Secretariat also provides some forms of legal assistance in the dispute settlement process and advises governments wishing to become members of the WTO. The annual budget is roughly 185 million Swiss francs.

THE WTO AGREEMENTS

The WTO agreements cover goods, services and intellectual property. They spell out the principles of liberalization, and the permitted exceptions. They include individual countries' commitments to lower customs tariffs and other trade barriers, and to open and keep open services markets. They set procedures for settling disputes. They

prescribe special treatment for developing countries. They require governments to make their trade policies transparent by notifying the WTO about laws in force and measures adopted, and through regular reports by the secretariat on countries' trade policies. These agreements are often called the WTO's trade rules, and the WTO is often described as "rules-based", a system based on rules. But it's important to remember that the rules are actually agreements that governments negotiated.

WTO Agreements deal with following issues.

For goods (under GATT)

- Agriculture
- Health regulations for farm products (SPS)
- Textiles and clothing
- Product standards (TBT)
- Investment measures
- Anti-dumping measures
- Customs valuation methods
- Pre-shipment inspection
- Rules of origin
- Import licensing
- Subsidies and counter-measures
- Safeguards

For services (the GATS annexes)

- Movement of natural persons
- Air transport
- Financial services
- Shipping
- Telecommunication

1. Agreement on Tariffs

There is no legally binding agreement that sets out the targets for tariff reductions (e.g. by what percentage they were to be cut as a result of the Uruguay Round). Instead, individual countries listed their commitments in schedules annexed to Marrakesh Protocol to the General Agreement on Tariffs and Trade 1994. This is the legally binding agreement for the reduced tariff rates. Since then, additional commitments were made under the 1997 Information Technology Agreement.

The agreement was to cut tarrifs. For developed countries' tariff cuts were for the most part phased in over five years from 1st January 1995. There was 40% cut in their tariffs on industrial products, from an average of 6.3% to 3.8%. The value of imported industrial products that receive duty-free treatment in developed countries jumped from 20% to 44%.

The fewer products charged high duty rates. The proportion of imports into developed countries from all sources

facing tariffs rates of more than 15% declined from 7% to 5%. The proportion of developing country exports facing tariffs above 15% in industrial countries fell from 9% to 5%.

The Uruguay Round package has been improved. On 26 March 1997, 40 countries accounting for more than 92% of world trade in information technology products, agreed to eliminate import duties and other charges on these products by 2000 (by 2005 in a handful of cases). As with other tariff commitments, each participating country is applying its commitments equally to exports from all WTO members (i.e. on a most-favoured-nation basis), even from members that did not make commitments.

The market access schedules in which tariff rates are announced by the countries represent commitments not to increase tariffs above the listed rates. The rates are "bound". For developed countries, the bound rates are generally the rates actually charged. Most developing countries have bound the rates somewhat higher than the actual rates charged, so the bound rates serve as ceiling rates.

2. The Agriculture Agreement

The objective of the Agriculture Agreement is to reform trade in the sector and to make policies more market-oriented. This would improve predictability and security for importing and exporting countries alike. The new rules and commitments apply to:

- market access – various trade restrictions confronting imports
- domestic support – subsidies and other programmes, including those that raise or guarantee farmgate prices and farmers' incomes
- export subsidies and other methods used to make exports artificially competitive.

The agreement allows governments to support their rural economies, but preferably through policies that cause less distortion to trade. It also allows some flexibility in the way commitments are implemented. Developing countries do not have to cut their subsidies or lower their tariffs as much as developed countries, and they are given extra time to complete their obligations. Least-developed countries don't have to do this at all. "Peace" provisions within the agreement aim to reduce the likelihood of disputes or challenges on agricultural subsidies over a period of nine years, until the end of 2003.

The new rule for market access in agricultural products is "tariffs only". Before the Uruguay Round, some agricultural imports were restricted by quotas and other non-tariff measures. These have been replaced by tariffs that provide more-or-less equivalent levels of protection. Converting the quotas and other types of measures to tariffs in this way was called "tariffication".

The Agriculture Agreement also distinguishes between support programmes that stimulate production directly, and those that are considered to have no direct effect.

Domestic policies that do have a direct effect on production and trade have to be cut back. Least-developed countries do not need to make any cuts. This category of domestic support is sometimes called the "amber box", a reference to the amber colour of traffic lights, which means "slow down". Measures with minimal impact on trade can be used freely – they are in a "green box" ("green" as in traffic lights). They include government services such as research, disease control, infrastructure and food security. Certain direct payments to farmers where the farmers are required to limit production (sometimes called "blue box" measures) were permitted.

The Agriculture Agreement prohibits export subsidies on agricultural products unless the subsidies are specified in a member's lists of commitments. Where they are listed, the agreement requires WTO members to cut both the amount of money they spend on export subsidies and the quantities of exports that receive subsidies. Under the Agriculture Agreement, WTO members have to reduce their subsidized exports.

3. Agreement on Standards and safety

Article 20 of the General Agreement on Trade (GATT) allows governments to act on order to protect human,

animal or plant health, provided they do not discriminate or use this as disguised protectionism. In addition, there are two specific WTO agreements dealing with food safety and animal and plant health and safety, and with product standards in general. Both try to identify how to meet the need to apply standards and at the same time avoid protectionism in disguise. These issues are becoming more important as tariff barriers fall – some compare this to seabed rocks appearing when the tide goes down. In both cases, if a country applies international standards, it is less likely to be challenged legally in the WTO than if it sets its own standards. A separate agreement on food safety and animal and plant health standards (the Sanitary and Phyto-sanitary Measures Agreement or SPS) sets out the basic rules. It allows countries to set their own standards. But it also says regulations must be based on science. They should be applied only to the extent necessary to protect human, animal or plant life or health. And they should not arbitrarily or unjustifiably discriminate between countries where identical or similar conditions prevail.

Member countries are encouraged to use international standards, guidelines and recommendations where they exist. Technical regulations and standards are important, but they vary from country to country. Having too many different standards makes life difficult for producers and exporters. Standards can become obstacles to trade. The Technical Barriers to Trade Agreement (TBT) tries to ensure that regulations, standards, testing and certification procedures do not create unnecessary obstacles. The agreement also sets out a code of good practice for both governments and non-governmental or industry bodies to prepare, adopt and apply voluntary standards. The Technical Barriers to Trade Committee is the major clearing house for members to share the information and the major forum to discuss concerns about the regulations and their implementation.

4. Agreement on Textiles

From 1974 until the end of the Uruguay Round, the trade was governed by the Multifibre Arrangement (MFA). This was a framework for bilateral agreements or unilateral actions that established quotas limiting imports into countries whose domestic industries were facing serious damage from rapidly increasing imports. The quotas were the most visible feature. Since 1995, the WTO's Agreement on Textiles and Clothing (ATC) took over from the Mulltifibre Arrangement. Textiles and clothing products were returned to GATT rules over the 10-year period. This happened gradually, in four steps, to allow time for both importers and exporters to adjust to the new situation. The agreement stated the percentage of products that had to be brought under GATT rules at each step. If any of these products came under quotas, then the quotas had to be removed at the same time. The percentages were applied to the importing country's textiles and clothing trade levels in 1990. The agreement also said the quantities of imports permitted under the quotas had to grow annually, and that the rate of expansion had to increase at each stage.

Products brought under GATT rules at each of the first three stages had to cover the four main types of textiles and clothing: tops and yarns; fabrics; made-up textile products; and clothing. Any other restrictions that did not come under the Multifibre Arrangement and did not conform with regular WTO agreements by 1996 had to be made to conform or be phased out by 2005.

These "transitional safeguards" were not the same as the safeguard measures normally allowed under GATT because they can be applied on imports from specific exporting countries. But the importing country had to show that its domestic industry was suffering serious damage or was threatened with serious damage. And it had to show that the damage was the result of two things: increased imports of the product in question from all sources, and a sharp and substantial increase from the specific exporting country. The safeguard restriction could be implemented either by mutual agreement following consultations, or unilaterally. It was subject to review by the Textiles Monitoring Body.

In any system where quotas are set for individual exporting countries, exporters might try to get around the quotas by shipping products through third countries or making false declarations about the products' country of origin. The agreement included provisions to cope with these cases.

The agreement envisaged special treatment for certain categories of countries – for example, new market entrants, small suppliers, and least-developed countries.

A Textiles Monitoring Body (TMB) supervised the agreement's implementation. It consisted of a chairman and 10 members acting in their personal capacity. It monitored actions taken under the agreement to ensure that they were consistent, and it reported to the Goods Council which reviewed the operation of the agreement before each new step of the integration process. The Textiles Monitoring Body also dealt with disputes under the Agreement on Textiles and Clothing. If they remained unresolved, the disputes could be brought to the WTO's regular Dispute Settlement Body. When the Textiles and Clothing Agreement expired on 1 January 2005, the Textiles Monitoring Body also ceased to exist.

5. Agreement on Trade in Services

The General Agreement on Trade in Services (GATS) is the first and only set of multilateral rules governing international trade in services. Negotiated in the Uruguay Round, it was developed in response to the huge growth of the services economy over the past 30 years and the greater potential for trading services brought about by the communications revolution. Services represent the fastest growing sector of the global economy and account for two thirds of global output, one third of global employment and nearly 20% of global trade. Following are the basic principles-

- All services are covered by GATS
- Most-favoured-nation treatment applies to all services, except the one-off temporary exemptions
- National treatment applies in the areas where commitments are made
- Transparency in regulations, inquiry points
- Regulations have to be objective and reasonable
- International payments: normally unrestricted
- Individual countries' commitments: negotiated and bound
- Progressive liberalization: through further negotiations

The agreement covers all internationally-traded services – for example, banking, telecommunications, tourism, professional services, etc. It also defines four ways (or "modes") of trading services:

- services supplied from one country to another (e.g. international telephone calls), officially known as "cross-border supply" (in WTO jargon, "mode 1")
- consumers or firms making use of a service in another country (e.g. tourism), officially "consumption abroad" ("mode 2")
- a foreign company setting up subsidiaries or branches to provide services in another country (e.g. foreign banks setting up operations in a country), offi-cially "commercial presence" ("mode 3")
- individuals travelling from their own country to supply services in another (e.g. fashion models or consultants), officially "presence of natural persons" ("mode 4").

Under GATS, if a country allows foreign competition in a sector, equal opportunities in that sector should be given to service providers from all other WTO members. MFN applies to all services, but some special temporary exemptions have been allowed. The commitments appear in "schedules" that list the sectors being opened, the extent of market access being given in those sectors (e.g. whether there are any restrictions on foreign ownership), and any limitations on national treatment. These clearly defined commitments are "bound": like bound tariffs for trade in goods, they can only be modified after negotiations with affected countries.

Transparency GATS says governments must publish all relevant laws and regulations, and set up enquiry points within their bureaucracies.

GATS does not require any service to be deregulated. Commitments to liberalize do not affect governments' right to set levels of quality, safety, or price, or to introduce regulations to pursue any other policy objective they see fit.

Once a government has made a commitment to open a service sector to foreign competition, it must not normally restrict money being transferred out of the country as payment for services supplied ("cur-rent transactions") in that sector.

6. Agreement on Intellectual Property

The WTO's Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), negotiated in the 1986–94 Uruguay Round, introduced intellectual property rules into the multilateral trading system for the first time.

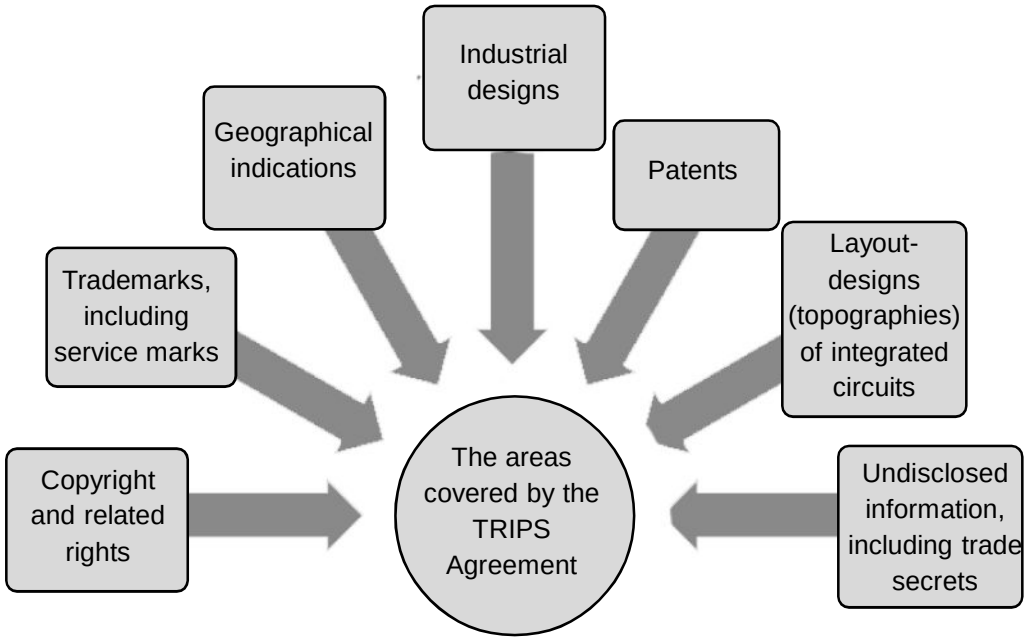
Ideas and knowledge are an increasingly important part of trade. Most of the value of new medicines and other high technology products lies in the amount of invention, innovation, research, design and testing involved. Creators can be given the right to prevent others from using their inventions, designs or other creations – and to use that right to negotiate payment in return for others using them. These are "intellectual property rights". They take a number of forms. For example books, paintings and films come under copyright; inventions can be patented; brandnames and product logos can be registered as trademarks; and so on. Governments and parliaments have given creators these rights as an incentive to produce ideas that will benefit society as a whole.

The extent of protection and enforcement of these rights varied widely around the world; and as intellectual property became more important in trade, these differences became a source of tension in international economic relations. New internationally agreed trade rules for intellectual property rights were seen as a way to introduce more order and predictability, and for disputes to be settled more systematically.

The Uruguay Round achieved that. The WTO's TRIPS Agreement is an attempt to narrow the gaps in the way these rights are protected around the world, and to bring them under common international rules. It establishes minimum levels of protection that each government has to give to the intellectual property of fellow WTO members. In doing so, it strikes a balance between the long term benefits and possible short term costs to society. Society benefits in the long term when intellectual property pro-tection encourages creation and invention, especially when the period of protection expires and the creations and inventions enter the public domain. Governments are allowed to reduce any short term costs through various exceptions, for example to tackle public health problems. And, when there are trade disputes over intellectual property rights, the WTO's dispute settlement system is now available.

The agreement covers five broad issues:

- how basic principles of the trading system and other international intellectual property agreements should be applied
- how to give adequate protection to intellectual property rights
- how countries should enforce those rights adequately in their own territories
- how to settle disputes on intellectual property between members of the WTO
- special transitional arrangements during the period when the new system is being introduced.



As in GATT and GATS, the starting point of the intellectual property agreement is basic principles. And as in the two other agreements, non-discrimination features prominently: national treatment (treating one's own nationals and foreigners equally), and most-favoured-nation treatment (equal treatment for nationals of all trading partners in the WTO). National treatment is also a key principle in other intellectual property agreements outside the WTO.

***The TRIPS Agreement has an additional important principle*:** intellectual property protection should contribute to technical innovation and the transfer of technology. Both producers and users should benefit, and economic and social welfare should be enhanced, the agreement says. The agreement also says governments have to ensure that intellectual property rights can be enforced under their laws, and that the penalties for infringement are tough enough to deter further violations. The procedures must be fair and equitable, and not unnecessarily complicated or costly.

***Copyright*:** The TRIPS agreement ensures that computer programs will be protected as literary works under the Berne Convention and outlines how databases should be protected. It also expands international copyright rules to cover rental rights. Authors of computer programs and producers of sound recordings must have the right to prohibit the commercial rental of their works to the public. A similar exclusive right applies to films where commercial rental has led to widespread copying, affecting copyright-owners' potential earnings from their films. The agreement says performers must also have the right to prevent unauthorized recording, reproduction and broadcast of live performances (bootlegging) for no less than 50 years. Producers of sound recordings must have the right to prevent the unauthorized reproduction of recordings for a period of 50 years.

***Trademarks*:** The agreement defines what types of signs must be eligible for protection as trade-marks, and what the minimum rights conferred on their owners must be. It says that service marks must be protected in the same way as trademarks used for goods. Marks that have become well-known in a particular country enjoy additional protection.

***Geographical indications*:** A place name is sometimes used to identify a product. This "geographical indication" does not only say where the product was made. More importantly it identifies the products special characteristics, which are the result of the product's origins.

Well-known examples include "Champagne", "Scotch", "Tequila", and "Roquefort" cheese. Wine and spirits makers are particularly concerned about the use of place-names to identify products, and the TRIPS Agreement contains special provisions for these products. But the issue is also important for other types of goods.

Using the place name when the product was made elsewhere or when it does not have the usual characteristics can mislead consumers, and it can lead to unfair com-petition. The TRIPS Agreement says countries have to prevent this misuse of place names.

For wines and spirits, the agreement provides higher levels of protection, i.e. even where there is no danger of the public being misled.

Some exceptions are allowed, for example if the name is already protected as a trade-mark or if it has become a generic term. For example, “cheddar” now refers to a par-ticular type of cheese not necessarily made in Cheddar, in the UK. But any country wanting to make an exception for these reasons must be willing to negotiate with the country which wants to protect the geographical indication in question.

The agreement provides for further negotiations in the WTO to establish a multilateral system of notification and registration of geographical indications for wines. These are now part of the Doha Development Agenda and they include spirits. Also debated in WTO, is whether to negotiate extending this higher level of protection beyond wines and spirits.

Industrial designs**:** Under the TRIPS Agreement, industrial designs must be protected for at least 10 years. Owners of protected designs must be able to prevent the manufacture, sale or importation of articles bearing or embodying a design which is a copy of the protected design.

Patents**:** The agreement says patent protection must be available for inventions for at least 20 years. Patent protection must be available for both products and processes, in almost all fields of technology. Governments can refuse to issue a patent for an invention if its commercial exploitation is prohibited for reasons of public order or morality. They can also exclude diagnostic, therapeutic and surgical methods, plants and animals (other than microorganisms), and biological processes for the production of plants or animals (other than microbiological processes).

If a patent is issued for a production process, then the rights must extend to the product directly obtained from the process.

Integrated circuits layout designs**:** The basis for protecting integrated circuit designs (“topographies”) in the TRIPS agreement is the Washington Treaty on Intellectual Property in Respect of Integrated Circuits, which comes under the World Intellectual Property Organization. This was adopted in 1989 but has not yet entered into force. The TRIPS agreement adds a number of provisions: for example, protection must be available for at least 10 years.

Undisclosed information and trade secrets: Trade secrets and other types of “undisclosed information” which have commercial value must be protected against breach of confidence and other acts contrary to honest commercial practices. But reasonable steps must have been taken to keep the information secret. Test data submitted to governments in order to obtain marketing approval for new pharmaceutical or agricultural chemicals must also be protected against unfair commercial use.

Curbing anti-competitive licensing contracts: The owner of a copyright, patent or other form of intellectual property right can issue a licence for someone else to produce or copy the protected trademark, work, invention, design, etc. The agreement recognizes that the terms of a licensing con-tract could restrict competition or impede technology transfer. It says that under certain conditions, governments have the right to take action to prevent anti-competitive licensing that abuses intellectual property rights. It also says governments must be prepared to consult each other on controlling anti-competitive licensing.

7. Agreement on Safeguards

A WTO member may restrict imports of a product temporarily (take “safeguard” actions) if its domestic industry is injured or threatened with injury caused by a surge in imports. Here, the injury has to be serious. Safeguard measures were always available under GATT (Article 19). However, they were infrequently used, some

governments preferring to protect their domestic industries through “grey area” measures – using bilateral negotiations outside GATT’s auspices, they per-suaded exporting countries to restrain exports “voluntarily” or to agree to other means of sharing markets. Agreements of this kind were reached for a wide range of products: automobiles, steel, and semiconductors, for example.

The WTO agreement broke new ground. It prohibits “grey-area” measures, and it sets time limits (a “sunset clause”) on all safeguard actions. The agreement says members must not seek, take or maintain any voluntary export restraints, orderly marketing arrangements or any other similar measures on the export or the import side. The bilateral measures that were not modified to conform with the agreement were phased out at the end of 1998. Countries were allowed to keep one of these measures an extra year (until the end of 1999), but only the European Union – for restrictions on imports of cars from Japan – made use of this provision.

An import “surge” justifying safeguard action can be a real increase in imports (an absolute increase); or it can be an increase in the imports’ share of a shrinking market, even if the import quantity has not increased (relative increase).

Industries or companies may request safeguard action by their government. The WTO agreement sets out requirements for safeguard investigations by national authorities. The emphasis is on transparency and on following established rules and practices – avoiding arbitrary methods. The authorities conducting investigations have to announce publicly when hearings are to take place and provide other appro-priate means for interested parties to present evidence. The evidence must include arguments on whether a measure is in the public interest.

The agreement sets out criteria for assessing whether “serious injury” is being caused or threatened, and the factors which must be considered in determining the impact of imports on the domestic industry. When imposed, a safeguard measure should be applied only to the extent necessary to prevent or remedy serious injury and to help the industry concerned to adjust. Where quantitative restrictions (quotas) are imposed, they normally should not reduce the quantities of imports below the annual average for the last three representative years for which statistics are available, unless clear justification is given that a different level is necessary to pre-vent or remedy serious injury.

In principle, safeguard measures cannot be targeted at imports from a particular country. However, the agreement does describe how quotas can be allocated among supplying countries, including in the exceptional circumstance where imports from certain countries have increased disproportionately quickly. A safeguard measure should not last more than four years, although this can be extended up to eight years, subject to a determination by competent national authorities that the mea-sure is needed and that there is evidence the industry is adjusting. Measures imposed for more than a year must be progressively liberalized.

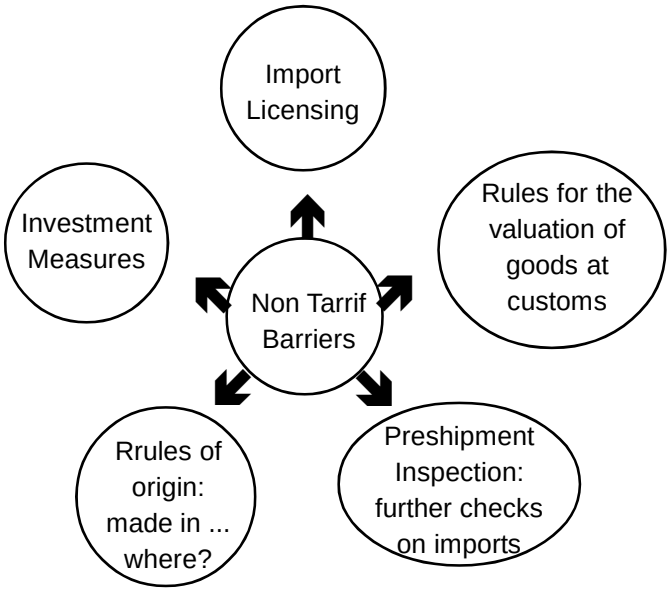
When a country restricts imports in order to safeguard its domestic producers, in principle it must give something in return. The agreement says the exporting country (or exporting countries) can seek compensation through consultations. If no agreement is reached the exporting country can retaliate by taking equivalent action – for instance, it can raise tariffs on exports from the country that is enforcing the safeguard measure. In some circumstances, the exporting country has to wait for three years after the safeguard measure was introduced before it can retaliate in this way – i.e. if the measure conforms with the provisions of the agreement and if it is taken as a result of an increase in the quantity of imports from the exporting country.

To some extent developing countries’ exports are shielded from safeguard actions. An importing country can only apply a safeguard measure to a product from a developing country if the developing country is supplying more than 3% of the imports of that product, or if developing country members with less than 3% import share collectively account for more than 9% of total imports of the product concerned.

The WTO’s Safeguards Committee oversees the operation of the agreement and is responsible for the surveillance of members’ commitments. Governments have to report each phase of a safeguard investigation and related decision-making, and the committee reviews these reports.

8. Agreements on Non-tariff Barriers: Red Tape, Etc

A number of agreements deal with various bureaucratic or legal issues that could involve hindrances to trade. These are called non tarrif barriers



***Import licensing*:** The Agreement on Import Licensing Procedures says import licensing should be simple, transparent and predictable. For example, the agreement requires governments to publish sufficient information for traders to know how and why the licences are granted. It also describes how countries should notify the WTO when they introduce new import licensing procedures or change existing procedures. The agreement offers guidance on how governments should assess applications for licences. Some licences are issued automatically if certain conditions are met. The agreement sets criteria for automatic licensing so that the procedures used do not restrict trade. Other licences are not issued automatically. Here, the agreement tries to minimize the importers' burden in applying for licences, so that the administrative work does not in itself restrict or distort imports. The agreement says the agencies handling licensing should not normally take more than 30 days to deal with an application – 60 days when all applications are considered at the same time.

***Rules for the valuation of goods at customs*:** The WTO agreement on customs valuation aims for a fair, uniform and neutral system for the valuation of goods for customs purposes – a system that conforms to commercial realities, and which outlaws the use of arbitrary or fictitious customs values. The agreement provides a set of valuation rules, expanding and giving greater precision to the provisions on customs valuation in the original GATT.

***Preshipment inspection*:** Preshipment inspection is the practice of employing specialized private companies to check shipment details – essentially price, quantity and quality – of goods ordered overseas. The Preshipment Inspection Agreement recognizes that GATT principles and obligations apply to the activities of preshipment inspection agencies mandated by governments. The obligations placed on governments which use preshipment inspections include non-discrimination, transparency, protection of confidential business information, avoiding unreasonable delay, the use of specific guidelines for conducting price veri-fication and avoiding conflicts of interest by the inspection agencies. The obligations of exporting members towards countries using preshipment inspection include non-discrimination in the application of domestic laws and regulations, prompt publication of those laws and regulations and the provision of technical assistance where requested. The agreement establishes an independent review procedure. This is administered jointly by the International Federation of Inspection Agencies (IFIA), representing inspection agencies, and the International Chamber of Commerce (ICC), representing exporters. Its purpose is to resolve disputes between an exporter and an inspection agency.

Rules of origin: made in ... where? "Rules of origin" are the criteria used to define where a product was made. They are an essential part of trade rules because a number of policies discriminate between exporting countries: quotas, preferential tariffs, anti-dumping actions, countervailing duty etc. Rules of origin are also used to compile trade statistics, and for "made in ..." labels that are attached to products. This is complicated by globalization and the way a product can be processed in several countries before it is ready for the market. Rules of Origin Agreement requires WTO members to ensure that their rules of origin are transparent; that they do not have restricting, distorting or disruptive effects on international trade; that they are administered in a consistent, uniform, impartial and reasonable manner; and that they are based on a positive standard (in other words, they should state what does confer origin rather than what does not). An annex to the agreement sets out a "common declaration" dealing with the operation rules of origin on goods which qualify for preferential treatment.

Investment measures: The Trade-Related Investment Measures (TRIMs) Agreement applies only to measures that affect trade in goods. It recognizes that certain measures can restrict and distort trade, and states that no member shall apply any measure that discriminates against foreigners or foreign products (i.e. violates "national treatment" principles in GATT). It also outlaws investment measures that lead to restrictions in quantities (violating another principle in GATT). An illustrative list of TRIMs agreed to be inconsistent with these GATT articles is appended to the agreement. The list includes measures which require particular levels of local procurement by an enterprise ("local content requirements"). It also discourages measures which limit a company's imports or set targets for the company to export ("trade balancing requirements").

Under the agreement, countries must inform fellow-members through the WTO of all investment measures that do not conform with the agreement. Developed countries had to eliminate these in two years (by the end of 1996); developing countries had five years (to the end of 1999); and least-developed countries seven. In July 2001, the Goods Council agreed to extend this transition period for a number of requesting developing countries.

9. Agreement on plurilaterals

For the most part, all WTO members subscribe to all WTO agreements. After the Uruguay Round, however, there remained four agreements, originally negotiated in the Tokyo Round, which had a narrower group of signatories and are known as "plurilateral agreements". All other Tokyo Round agreements became multilateral obligations (i.e. obligations for all WTO members) when the World Trade Organization was established in 1995. The four were:

- trade in civil aircraft
- government procurement
- dairy products and
- bovine meat.

The bovine meat and dairy agreements were terminated in 1997.

Fair trade in civil aircraft: The Agreement on Trade in Civil Aircraft entered into force on 1 January 1980. It now has 30 signatories. The agreement eliminates import duties on all aircraft, other than military aircraft, as well as on all other products covered by the agreement civil aircraft engines and their parts and components, all components and sub-assemblies of civil aircraft, and flight simulators and their parts and components. It contains disciplines on government-directed procurement of civil aircraft and inducements to purchase, as well as on government financial support for the civil aircraft sector.

Government procurement: In most countries the government, and the agencies it controls, are together the biggest purchasers of goods of all kinds, ranging from basic commodities to high-technology equipment. At the same time, the political pressure to favour domestic suppliers over their foreign competitors can be very strong. An Agreement on Government Procurement was first negotiated during the Tokyo Round and entered into force on 1 January 1981. Its purpose is to open up as much of this business as possible to international competition.

It is designed to make laws, regulations, procedures and practices regarding government procurement more transparent and to ensure they do not protect domestic products or suppliers, or discriminate against foreign products or suppliers.

The agreement has 28 members. It has two elements – general rules and obligations, and schedules of national entities in each member country whose procure-ment is subject to the agreement. A large part of the general rules and obligations concern tendering procedures.

The present agreement and commitments were negotiated in the Uruguay Round. These negotiations achieved a 10-fold expansion of coverage, extending international competition to include national and local government entities whose collective purchases are worth several hundred billion dollars each year. The new agreement also extends coverage to services (including construction services), procurement at the sub-central level (for example, states, provinces, departments and prefectures), and procurement by public utilities. The new agreement took effect on 1 January 1996.

It also reinforces rules guaranteeing fair and non-discriminatory conditions of inter-national competition. For example, governments will be required to put in place domestic procedures by which aggrieved private bidders can challenge procurement decisions and obtain redress in the event such decisions were made inconsistently with the rules of the agreement. The agreement applies to contracts worth more than specified threshold values.

10. Agreement on Trade Policy Reviews

This agreement is called Trade Policy Review Mechanism. Individuals and companies involved in trade have to know as much as possible about the conditions of trade. It is therefore fundamentally important that regulations and policies are transparent. In the WTO, this is achieved in two ways: governments have to inform the WTO and fellow-members of specific measures, policies or laws through regular “notifications”; and the WTO conducts regular reviews of individual countries’ trade policies – the trade policy reviews. These reviews are part of the Uruguay Round agreement, but they began several years before the round ended – they were an early result of the negotiations. Participants agreed to set up the reviews at the December 1988 ministerial meeting that was intended to be the midway assessment of the Uruguay Round. The first review took place the following year. Initially they operated under GATT and, like GATT, they focused on goods trade. With the creation of the WTO in 1995, their scope was extended, like the WTO, to include services and intellectual property. The objectives are:

- to increase the transparency and understanding of countries’ trade policies and practices, through regular monitoring
- improve the quality of public and intergovernmental debate on the issues
- to enable a multilateral assessment of the effects of policies on the world trading system.

The reviews focus on members’ own trade policies and practices. But they also take into account the countries’ wider economic and developmental needs, their policies and objectives, and the external economic environment that they face. These “peer reviews” by other WTO members encourage governments to follow more closely the WTO rules and disciplines and to fulfill their commitments. In practice the reviews have two broad results: they enable outsiders to understand a country’s policies and circumstances, and they provide feedback to the reviewed country on its performance in the system.

Over a period of time, all WTO members are to come under scrutiny. The frequency of the reviews depends on the country’s size:

- The four biggest traders – the European Union, the United States, Japan and China – are examined approximately once every two years.
- The next 16 countries (in terms of their share of world trade) are reviewed every four years.

– The remaining countries are reviewed every six years, with the possibility of a longer interim period for the least-developed countries.

For each review, two documents are prepared: a policy statement by the government under review, and a detailed report written independently by the WTO Secretariat. These two reports, together with the proceedings of the Trade Policy Review Body's meetings are published shortly afterwards.

11. Agreement on Anti-Dumping Duties – Discussed in Chapter 8 of this Book.

12. Agreement on Subsidies and Counter Value Measures – Discussed in Chpater 9 of this Book.

Recent WTO Negotiations and India

The Doha Round of trade negotiations in the WTO which began in 2001 remains unfinished due to differences among members on various issues.

The Eighth Ministerial Meeting of the WTO which was held in December 2011 in Geneva provided political guidance to the members to resolve the issues involved. However, there was no significant progress in 2012.

Efforts are being made for an early harvest on some issues in time for the Ninth Ministerial Conference of the WTO (MC9) to be held in December 2013. India is of the view that any early outcome of the negotiations should invariably address issues of interest to the developing countries, especially the least developed countries (LDCs) and the small vulnerable economies (SVEs).

A Draft Consolidated Negotiating Text on Trade Facilitation was worked out by the WTO members on 14 December 2009. The Draft Text has since been revised fourteen times (till December 2012) through discussions in the meetings of the Negotiating Group on Trade Facilitation (NGTF). India is actively engaged in these negotiations and has also tabled a few proposals on 'Customs Cooperation', 'Rapid Alerts System of Customs Union', and 'Appeal Mechanism'. The Draft Text, however, lacks internal balance.

The developed countries are holding up the laws and procedures of their own countries as benchmarks and want the developing countries to replicate them. Developing countries have by and large adopted a defensive approach in the negotiations. The developed countries and a few developing countries are making efforts to harvest 'Trade facilitation' for an early outcome, in time for MC9.

India along with most of the developing countries wants issues of market access and trade facilitation to be balanced with developmental issues such as duty free quota, free market access for LDCs, and acceptance of the modalities for reducing cotton subsidies.

The G33 group of countries, which is a coalition of 46 developing countries, including India, has tabled a proposal on food security in the WTO on 16 November 2012. The proposal is for an amendment to certain provisions of the WTO Agreement on Agriculture to allow developing countries greater flexibility in their public stockholding operations for food security purposes. The issue of food security is very important for India and any concession on the trade facilitation front needs to be balanced by acceptance of the G33 proposal in any package deal for MC9.

Negotiations in services have continued primarily in the plurilateral format. Intensive negotiations were held in 2009, 2010, and also till the first half of 2011.These efforts culminated in a report by the Chair of the Committee on Trade in Services - Special Session (CTS-SS) and all subsidiary bodies under the CTS in April 2011.

The Chair's report puts forth two views. The developed countries' view is that further progress on market access could include the binding of autonomous liberalization where possible, improved levels of access under commercial presence mode, that is, Mode 3 (including restrictions on foreign equity participation and forms of commercial presence), as well as a robust and satisfactory outcome in Mode 4 (presence of natural persons).

The developing countries' view is that there is an imbalance in market access negotiations, as evidenced by the fact that developing country flexibilities have not been taken into account in other members' requests, sectors of export interest to developing countries are not being fully reflected in developed members' offers; developing countries have already made a significant contribution to the Doha Round; and some plurilateral requests and recent proposals have embodied a level of ambition going beyond that agreed in Annex C of the Hong Kong Ministerial Declaration. India has already made considerable improvement in its revised offer (from 37 sub-sectors in the Uruguay Round to 95 in the Revised Offer). Some of the major developed country members have shown nil or little movement in their Mode 4 offers.

UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT (UNCTAD)

UNCTAD was established in 1964 to promote the development-friendly integration of developing countries into the world economy. UNCTAD has progressively evolved into an authoritative knowledge-based institution whose work aims to help shape current policy debates and thinking on development, with a particular focus on ensuring that domestic policies and international action are mutually supportive in bringing about sustainable development. The organization works to fulfill this mandate by carrying out three key functions-

- It functions as a forum for intergovernmental deliberations, supported by discussions with experts and exchanges of experience, aimed at consensus building.
- It undertakes research, policy analysis and data collection for the debates of government representatives and experts.
- It provides technical assistance tailored to the specific requirements of developing countries, with special attention to the needs of the least developed countries and of economies in transition. When appropriate, UNCTAD cooperates with other organizations and donor countries in the delivery of technical assistance.

The Secretary-General of UNCTAD is Dr. Supachai Panitchpakdi (Thailand), who took office on 1 September 2005. In performing its functions, the secretariat works together with member Governments and interacts with organizations of the United Nations system and regional commissions, as well as with governmental institutions, non-governmental organizations, the private sector, including trade and industry associations, research institutes and universities worldwide.

In late 2011, the UNCTAD Secretary-General reconvened the UNCTAD Panel of Eminent Persons to advise him on how to meet the key and emerging economic development challenges of today, and provide concrete ideas for international initiatives on how to deal with them, and how to strategically position UNCTAD in this context.

As recognized in its founding mandate, UNCTAD is the focal point of the United Nations for the integrated treatment of trade, investment, technology, finance, commodities and interrelated issues, in advancing inclusive growth and sustainable development.

Members

Following 194 countries are member of UNCTAD.

Afghanistan	Armenia	Barbados
Albania	Australia	Belarus
Algeria	Austria	Belgium
Andorra	Azerbaijan	Belize
Angola	Bahamas	Benin
Antigua and Barbuda	Bahrain	Bhutan
Argentina	Bangladesh	Bolivia

Bosnia and Herzegovina	Finland	Libyan Arab Jamahiriya
Botswana	France	Liechtenstein
Brazil	Gabon	Lithuania
Brunei Darussalam	Gambia	Luxembourg
Bulgaria	Georgia	Madagascar
Burkina Faso	Germany	Malawi
Burundi	Ghana	Malaysia
Cambodia	Greece	Maldives
Cameroon	Grenada	Mali
Canada	Guatemala	Malta
Cape Verde	Guinea	Marshall Islands
Central African Republic	Guinea-Bissau	Mauritania
Chad	Guyana	Mauritius
Chile	Haiti	Mexico
China	Holy See	Micronesia (Federated States of)
Colombia	Honduras	Moldova
Comoros	Hungary	Monaco
Congo	Iceland	Mongolia
Costa Rica	India	Montenegro
Côte d´Ivoire	Indonesia	Morocco
Croatia	Iran (Islamic Republic of)	Mozambique
Cuba	Iraq	Myanmar
Cyprus	Ireland	Namibia
Czech Republic	Israel	Nauru
Democratic People´s Republic of Korea	Italy	Nepal
Democratic Republic of the Congo	Jamaica	Netherlands
Denmark	Japan	New Zealand
Djibouti	Jordan	Nicaragua
Dominica	Kazakhstan	Niger
Dominican Republic	Kenya	Nigeria
Ecuador	Kiribati	Norway
Egypt	Kuwait	Oman
El Salvador	Kyrgyzstan	Pakistan
Equatorial Guinea	Lao People´s Democratic Republic	Palau
Eritrea	Latvia	Panama
Estonia	Lebanon	Papua New Guinea
Ethiopia	Lesotho	Paraguay
Fiji	Liberia	Peru
		Philippines
		Poland

Portugal	Slovenia	Trinidad and Tobago
Qatar	Solomon Islands	Tunisia
Republic of Korea	Somalia	Turkey
Romania	South Africa	Turkmenistan
Russian Federation	South Sudan	Tuvalu
Rwanda	Spain	Uganda
Saint Kitts and Nevis	Sri Lanka	Ukraine
Saint Lucia	Sudan	United Arab Emirates
Saint Vincent and the Grenadines	Suriname	United Kingdom of Great Britain and Northern Ireland
Samoa	Swaziland	United Republic of Tanzania
San Marino	Sweden	United States of America
Sao Tome and Principe	Switzerland	Uruguay
Saudi Arabia	Syrian Arab Republic	Uzbekistan
Senegal	Tajikistan	Vanuatu
Serbia	Thailand	Venezuela
Seychelles	The Former Yugoslav Republic of Macedonia	Viet Nam
Sierra Leone	Timor-Leste	Yemen
Singapore	Togo	Zambia
Slovakia	Tonga	Zimbabwe

UNCTAD Conferences

The highest decision-making body of UNCTAD is the quadrennial conference, at which member States make assessments of current trade and development issues, discuss policy options and formulate global policy responses. The conference also sets the organization's mandate and work priorities.

- The conference is a subsidiary organ of the United Nations General Assembly.
- The conferences serve an important political function: they allow intergovernmental consensus building regarding the state of the world economy and development policies, and they play a key role in identifying the role of the United Nations and UNCTAD in addressing economic development problems.

HIstory of UNCTAD

Foundation

- In the early 1960s, growing concerns about the place of developing countries in international trade led many of these countries to call for the convening of a full-fledged conference specifically devoted to tackling these problems and identifying appropriate international actions.
- The first United Nations Conference on Trade and Development (UNCTAD) was held in Geneva in 1964. Given the magnitude of the problems at stake and the need to address them, the conference was institutionalized to meet every four years, with intergovernmental bodies meeting between sessions and a permanent secretariat providing the necessary substantive and logistical support.
- Simultaneously, the developing countries established the Group of 77 to voice their concerns. (Today, the G77 has 131 members.)

- The prominent Argentinian economist Raúl Prebisch, who had headed the United Nations Economic Commission for Latin America and the Caribbean, became the organization's first Secretary-General.

Phase 1: The 1960s and 1970s

- In its early decades of operation, UNCTAD gained authoritative standing:
  - as an intergovernmental forum for North-South dialogue and negotiations on issues of interest to developing countries, including debates on the "New International Economic Order".
  - for its analytical research and policy advice on development issues.
- Agreements launched by UNCTAD during this time include:
  - the Generalized System of Preferences (1968), whereby developed economies grant improved market access to exports from developing countries.
  - a number of International Commodities Agreements, which aimed at stabilizing the prices of export products crucial for developing countries.
  - the Convention on a Code of Conduct for Liner Conferences, which strengthened the ability of developing countries to maintain national merchant fleets.
  - the adoption of a Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices. This work later evolved into what is today known as "Trade and Competition Policies".
- Furthermore, UNCTAD was a key contributor to:
  - the definition of the target of 0.7% of gross domestic product (GDP) to be given as official development aid by developed countries to the poorest countries, as adopted by the United Nations General Assembly in 1970.
  - the identification of the Group of Least Developed Countries (LDCs) as early as 1971, which drew attention to the particular needs of these poorest countries. UNCTAD became the focal point within the UN system for tackling LDC-related economic development issues.

Phase 2: The 1980s

- In the 1980s, UNCTAD was faced with a changing economic and political environment:
  - There was a significant transformation in economic thinking. Development strategies became more market-oriented, focusing on trade liberalization and privatization of state enterprises.
  - A number of developing countries were plunged into severe debt crises. Despite structural adjustment programs by the World Bank and the International Monetary Fund, most developing countries affected were not able to recover quickly. In many cases, they experienced negative growth and high rates of inflation. For this reason, the 1980s become known as the "lost decade", particularly in Latin America.
  - Economic interdependence in the world increased greatly.
- In the light of these developments, UNCTAD multiplied efforts aimed at:
  - strengthening the analytical content of its intergovernmental debate, particularly regarding macroeconomic management and international financial and monetary issues.
  - broadening the scope of its activities to assist developing countries in their efforts to integrate into the world trading system. In this context, the technical assistance provided by UNCTAD to developing countries was particularly important in the Uruguay Round of trade negotiations, which had begun

under the General Agreement on Tariffs and Trade (GATT) in 1986. UNCTAD played a key role in supporting the negotiations for the General Agreement on Trade in Services (GATS). UNCTAD's work on trade efficiency (customs facilitation, multimodal transport) made an important contribution to enabling developing economies to reap greater gains from trade. UNCTAD assisted developing countries in the rescheduling of official debt in the Paris Club negotiations.

- promoting South-South cooperation. In 1989, the Agreement on the Global System of Trade Preferences among Developing Countries (GSTP) came into force. It provided for the granting of tariff as well as non-tariff preferences among its members. To date, the Agreement has been ratified by 44 countries.
- addressing the concerns of the poorest nations by organizing the first UN Conference on Least Developed Countries in 1981. Since then, two other international conferences have been held at 10-year intervals.

Phase 3: From the 1990s until today

- Key developments in the international context:
  - The conclusion of the Uruguay Round of trade negotiations under the GATT resulted in the establishment of the World Trade Organizationin 1995, which led to a strengthening of the legal framework governing international trade.
  - A spectacular increase in international financial flows led to increasing financial instability and volatility.
  - Against this background, UNCTAD's analysis gave early warning concerning the risks and the destructive impact offinancial crises on development. Consequently, UNCTAD emphasized the need for a more development-oriented "international financial architecture".
  - Foreign direct investment flows became a major component of globalization.
  - UNCTAD highlighted the need for a differentiated approach to the problems of developing countries. Its tenth conference, held in Bangkok in February 2000, adopted a political declaration – "The Spirit of Bangkok" – as a strategy to address the development agenda in a globalizing world.
- In recent years, UNCTAD has
  - further focused its analytical research on the linkages between trade, investment, technology and enterprise development.
  - put forward a "positive agenda" for developing countries in international trade negotiations, designed to assist developing countries in better understanding the complexity of the multilateral trade negotiations and in formulating their positions.
  - Expanded work on international investment issues, following the merger into UNCTAD of the New York–based United Nations Centre on Transnational Corporations in 1993.
  - expanded and diversified its technical assistance, which today covers a wide range of areas, including training trade negotiators and addressing trade-related issues; debt management, investment policy reviews and the promotion of entrepreneurship; commodities; competition law and policy; and trade and environment.

Main Goals

- To work as a laboratory of ideas and to provide on-the-ground assistance to help developing countries raise living standards through trade, investment, finance and technology
- To help developing countries benefit from the globalized economy

– To contribute to international debate on emerging issues related to developing countries and the world economy - such as the current global financial crisis - through major reports, policy briefs, and contributions to international conferences.

Main Activities

1. Globalization and Development Strategies

– Identify broad trends and prospects in the world economy, such as the recent rise in "South-South" trade

– Identify solutions to the economic development challenges of African countries

– Analyse the effects on least developed countries of international aid and of other efforts to promote development

– Help with the restructuring of developing-country debt

2. Trade in Goods and Services

– Assist developing countries in all aspects of their trade negotiations

– Analyse the impact of competition laws and policies on development

– Encourage the inclusion of environmental issues, such as climate change and preservation of biodiversity, in trade and development policies

3. Commodities

– Examine the factors influencing commodity markets

– Help developing country efforts to achieve sustainable commodity exportst

– Help commodity-dependent countries diversify their economies

4. Investment and Enterprise Development

– Analyse trends in foreign direct investment and their impacts on development

– Help countries participate in international investment agreements

– Advise governments on their investment policies through investment policy reviews, guides, and training

– Help with the creation and nurturing of small and medium-sized enterprises

– Help countries establish and observe international standards for accounting

5. Trade Logistics and Human Resource Development

– Partner with Developing Countries to address Transport and Trade Facilitation challenges and opportunities

– Technical assistance in Trade Facilitation reforms and Customs automation

– Cooperation in Transit transport systems for landlocked and transit developing countries

– Research in Maritime and Sustainable Transport

– Legal and Regulatory Transport related issues

– Build training networks and organize training in all areas of international trade, in particular for least developed countries

Relationship with Other Agencies

As the focal point for the integrated treatment of trade and development, UNCTAD interacts and cooperates with a variety of other organizations within and outside the United Nations system. These include the following:

1. World Trade Organization

UNCTAD and WTO have been joining forces to ensure a better functioning of the multilateral trading system. In April 2003, the organizations signed a Memorandum of Understanding providing for cooperation and consultations on their technical assistance activities and for the conduct of joint studies on selected issues. UNCTAD and WTO interact frequently, and the intergovernmental processes in both organizations are often attended by the same Government representatives.

2. International Trade Centre

The ITC is jointly sponsored by UNCTAD and WTO for operational, enterprise-oriented aspects of trade development, with an emphasis on trade promotion. In contrast to UNCTAD, whose technical assistance is primarily tailored to Governments, ITC's technical assistance focuses on assisting businesses in developing countries. Both UNCTAD and WTO are represented in the Joint Advisory Group supervising ITC's work, and UNCTAD has a number of joint technical assistance activities with ITC.

3. UN Regional Commissions and UNDP

UNCTAD cooperates with these international entities on a project-by-project basis, be it in relation to research projects, joint workshops and seminars, or technical assistance. Since UNCTAD has no representatives in the field, the UNDP country offices are also used to support UNCTAD activities in various countries.

4. UN Inter-Agency Cluster on trade and productive capacity

The CEB Inter-Agency Cluster on Trade and Productive Capacity is an interagency mechanism dedicated to the coordination of trade and development operations at the national and regional levels within the UN system.

The Cluster, makes a concrete and direct contribution to the UN system-wide coherence reform by coordinating its participation in the:

- Delivering as One UN Pilots and countries involved in a new UNDAF process, and
- United Nations Development Group (UNDG) machinery, in view of the formulation of new United Nations rules and standard mechanisms for development operations.

5. Bretton Woods institutions (International Monetary Fund and World Bank)

The World Bank and UNCTAD cooperate in the delivery of some technical assistance and capacity-building programmes. The UNCTAD secretariat, through the Debt Management–DMFAS programme, is also an active member of the Inter-Agency Task Force on Finance Statistics, which is chaired by the IMF. The three agencies also cooperate in organizing seminars. UNCTAD attends the biannual meetings of the IMF and the World Bank, and both institutions participate in UNCTAD's intergovernmental meetings.

6. Other intergovernmental bodies

In addition to the organizations of the UN system, a total of 111 other intergovernmental bodies have gained accreditation as observers to UNCTAD's Trade and Development Board.

UNCTAD and Civil Society

UNCTAD believes that enhanced cooperation between the private and the public sector is essential to the

effective integration of developing countries into the global economy and seeks ways to involve civil society organizations, academia, trade unions, parliamentarians and business associations in its work. Cooperation with civil society is mutually beneficial: it helps civil society actors, empowering and enhancing their advocacy role in support of sustainable development, while adding value to the work of UNCTAD and its member States in achieving tangible development outcomes. The Civil Society Outreach (CSO) Unit of UNCTAD is responsible for liaison and outreach to civil society. Its role is to encourage and facilitate participation and engagement of civil society in the work of UNCTAD.

This includes:

- Organizing the annual UNCTAD Public Symposium
- Organizing civil society activities and events at UNCTAD Conferences
- Organizing hearings, consultations, briefings and informal meetings with experts and civil society
- Reviewing and processing requests for accreditation and observer status with UNCTAD
- Providing civil society with relevant information and documentation on UNCTAD activities
- Liaising and interacting with other UN system focal points for civil society.

UNCTAD´S Programme Budget and Financing of Technical Cooperation Activities

The Secretariat is composed of about 400 staff members with an annual regular budget of approximately $68 million from the United Nations and $40 million of extra-budgetary technical assistance funds.

UNCTAD technical cooperation activities are financed from three main sources:

- Trust funds (i.e. voluntary contributions from donors)
- United Nations Development Programme (UNDP)
- United Nations programme budget

Evaluation at UNCTAD

The UNCTAD Evaluation and Monitoring Unit coordinates the oversight activities within the organization that serve to both ensure and enhance the quality and resonance of its programmes and projects. The main activities of the unit to cover this mandate include:

- Managing, conducting and supporting the evaluation activities of UNCTAD.
- Participating and contributing to inter-agency initiatives on evaluation, such as setting up evaluation standards or evaluation guidance materials.
- Providing guidance and assistance to programme managers in using results-based management methodologies, in particular providing input into the definition of results frameworks and in the preparation of programme performance reports.
- Participating in the review of new project proposals with a view to ensuring the evaluability of each project's logical framework, as a member of the Project Review Committee and through the clearance of project documents.
- Contributing to developing capacity for self-evaluations.
- Acting as the focal point for UNCTAD on all evaluation matters, in particular, external evaluations conducted by OIOS.

INTERNATIONAL COMMODITY AGREEMENTS

International commodity agreement is an agreement among producing and consuming countries to improve the functioning of the global market for a commodity. It may be administrative, providing information, or economic, influencing world price, usually using a buffer stock to stabilize it. An international commodity agreement is an undertaking by a group of countries to stabilize trade, supplies, and prices of a commodity for the benefit of participating countries. An agreement usually involves a consensus on quantities traded, prices, and stock management. A number of international commodity agreements serve solely as forums for information exchange, analysis, and policy discussion.

Objectives:

- To bring about co-ordination in the production and marketing of agreed commodities.
- To promote technical co-operation amongst members.
- To bring about remunerative and stable prices for the commodities.

International Commodity Agreements are overseen by UNCTAD. In its Final Act, the UNCTAD-I made a comprehensive statement on the functions of International Commodity Agreements. "The commodity agreements should have the objective of stimulating a dynamic and steady growth and ensuring reasonable predictability in the real export earnings of the developing countries so as to provide them with expanding resources for their economic and social development , while taking into account the interest of consumers in importing countries through remunerative, equitable and stable prices for primary commodities, having due regard to their import purchasing power, assured satisfactory access and increased imports and consumption as well as coordination of production and marketing policies."

International Commodity Agreement are inter governmental arrangements regulating the production of & trade in certain primary products for the purpose of stablising their prices.

International Commodity Agreements may take following forms:

International Buffer Stock Agreements

Any attempt to use commodity storage for the purposes of stabilizing prices in an economy or, an individual (commodity) market comes under buffer stock scheme. This is commonly implemented as 'intervention storage' or 'ever-normal granary'. They seek to stablise commodity prices by maintaining the demand – Supply balance.

When there is a surplus in the economy, the commodities are bought & stored and sold when shortage occurs in the economy.

Buffer stock agreements stablise the price by increasing the market supply by the sale of the commodity when the price trends to rise and by absorbing the excess supply to prevent a fall in the price.

The buffer stock schemes have a common platform, they work on similar lines with the two prices being determined i.e. (minimum and maximum price). A further fall in the price is ensured by the scheme operator (usually government) buying up the stock as the price drops close to the floor price. The operator depresses the price by selling off its holding when the price rises close to the ceiling. Inflation can be prevented if a basket of commodities is stored.

The buffer stock plan thus, requires an international agency to set a range of prices and to buy the commodity at the minimum and sell at the maximum. The buffer pool method has been tried in commodities like tin, cocoa & sugar. These buffer stock arrangement can be affected only for those products which can be stored at relatively low cost without the danger of deterioration. Further it also requires large financial resources to stock the commodity.

International Export Quota Agreement

International quota agreements seek to prevent a fall in commodity price by regulating their supply. Under this, the export quotas are determinated and allocated to participating countries according to some mutually agreed formula and they undertake to restrict the export or production by a certain percentage of the basic quota decided by the committee for instance in coffee agreement the major producers limited the amount that could be exported by each country. Export Quotas can be set by governments on domestic producers of goods or property putting restrictions on exports of a country, either voluntarily or at the request of other countries. Reasons for export quota agreement may be:

- the protection of domestic industry to the shortage of raw materials,
- to protect the local population's lack of food or other essentials,
- the maintenance of international awards raw materials or orderly marketing
- a voluntary export restraint agreement with the members of a cartel of producers (like OPEC) or
- the voluntary restraint agreements with countries export consumers.

The most important factor in determining whether a country imports or exports is the price of a product. The world price is the price prevailing on the world market. Domestic price is the price in a particular country. The goods whose world price is higher than the domestic price before trade, then the country will export the good. If the world price is below the domestic price before trade, then the country will import the good. The agreement gives the opportunity to purchase goods at lower prices from international market and sell them at a higher price in the domestic market.

Tariffs raise the domestic price above the world price by the amount of the tariff. The rise in domestic prices will lead to a decrease in domestic quantity demanded, and an increase in domestic supply. Quotas are restrictions on the maximum amount that can be imported, and has the same effect as tariffs do. They limit the number of domestic consumers and raise the price when the pressure drops similar to that of the rate.

Some International Commodity Agreements:

- International Grain Agreement
- Association of Natural Rubber Producing Countries
- International Coffee Agreement
- International Tropical Timber Agreement
- International Cotton Advisory Committee
- International Cocoa Agreement
- International Jute Council
- International Sugar Agreement

International Grains Agreement

The International Grains Agreement (IGA), which replaced the International Wheat Agreement in 1995, comprises a Grains Trade Convention (GTC) and a Food Aid Convention (FAC). The IGA is administered by the International Grains Council (IGC), an intergovernmental forum for cooperation on wheat and coarse grain matters.

The Grains Trade Convention provides for information-sharing, analysis and consultations on grain market and policy developments. Under the Food Aid Convention, donor countries pledge to provide annually specified amounts of food aid to developing countries in the form of grain suitable for human consumption, or cash to buy suitable grains in recipient countries. The International Grains Agreement does not contain any mechanisms for stabilizing supplies, prices, or trade.

International Coffee Agreement

The International Coffee Organization (ICO) is the main intergovernmental organization for coffee. ICO exporting members account for more than 97 percent of world coffee production, and its importing Members, are responsible for around 80 percent of world coffee consumption. The ICO makes a practical contribution to the world coffee economy and to the improvement of living standards in developing countries by facilitating intergovernmental consultation and coordination regarding coffee policies and priorities, by encouraging a sustainable world coffee economy, by initiating coffee development projects to add value and improve marketing, by increasing world coffee consumption through innovative market development activities, by promoting the improvement of coffee quality, by working closely with the global coffee industry through a 16 member Private Sector Consultative Board, and by ensuring transparency in the coffee market with objective and comprehensive information on the world coffee sector by means of statistics and market studies.

The United States led recent efforts to renegotiate the ICA, and the text of the seventh International Coffee Agreement (ICA 2007) was adopted by the International Coffee Council on September 28, 2007. The new ICA is designed to enhance the ICO's role as a forum for intergovernmental consultations, to increase its contributions to meaningful market information and market transparency, and to ensure that the organization plays a unique role in developing innovative and effective capacity building in the coffee sector. Among the features of the new agreement is a first-ever "Consultative Forum on Coffee Sector Finance" to promote the development and dissemination of innovations and best practices that can enable coffee producers to better manage financial aspects of the inherent volatility and risks associated with competitive and evolving markets. Other notable changes include expanding the organization's work in providing relevant statistical and market information and strengthening efforts to develop, review and implement capacity building projects that are particularly important to small-scale farmers in key developing country trading partners.

International Tropical Timber Agreement

The International Tropical Timber Agreement (ITTA) is often described as a "hybrid" agreement because it combines a traditional commodity trade agreement with objectives that include sustainable management of tropical forests. The ITTA established the International Tropical Timber Organization (ITTO), an intergovernmental organization with 59 members who collectively account for about 80 percent of the world's tropical forests and 90 percent of the annual trade in tropical timber trade. The ITTO promotes market transparency by collecting, analyzing and disseminating data on the production and trade of tropical timber; assists in developing, funding and implementing projects and other activities to build capacity to sustainably manage and use tropical forests; and facilitates intergovernmental consultation and international co-operation on issues relating to the trade and utilization of tropical timber and the sustainable management of its resource base.

Negotiations for a successor agreement to the ITTA 1994 were concluded in 2006, and the new agreement (ITTA 2006) is expected to further strengthen efforts to promote tropical timber trade in the context of sustainable management of tropical forests.

International Cotton Advisory Committee

The International Cotton Advisory Committee (ICAC) is an association of governments of cotton producing, consuming and trading countries which acts as the international commodity body for cotton and cotton textiles.

Founded at the International Cotton Meeting in Washington, DC in 1939, the ICAC advocates for cotton producing nations, publishes studies and technical information on the cotton industry, and holds an annual Plenary Meeting of member states. Its 2008 Plenary Meeting, the 67th, was held in Ouagadougou, Burkina Faso in 2008.[1] While most of the world's cotton producing nations are members, two of the ten largest producers (The Peoples Republic of China and Turkmenistan) are not members of the ICAC. All of the top five cotton exporting nations are members.

International Cocoa Agreement

The International Cocoa Organization (ICCO) is a global organization, composed of both cocoa producing and cocoa consuming countries with a membership. Located in London, ICCO was established in 1973 to put into effect the first International Cocoa Agreement which was negotiated in Geneva at a United Nations International Cocoa Conference. There have since been six Agreements. The Sixth International Cocoa Agreement was negotiated in Geneva in 2001 and came into force provisionally on 1 October 2003.

On 2 November 2005, the total percentage of exporting countries which had acceded to the Agreement surpassed 80%. Thus, the International Cocoa Agreement, 2001 entered into force definitively for the first time in the 30 year history of the International Cocoa Agreements. ICCO Member countries represent almost 85% of world cocoa production and more than 60% of world cocoa consumption. All Members are represented in the International Cocoa Council, the highest governing body of the ICCO.

The two most important breakthroughs of the present International Cocoa Agreement were the establishment of an explicit mandate on a Sustainable World Cocoa Economy and the founding of the Consultative Board on the World Cocoa Economy.

The Consultative Board consists of fourteen international experts in the cocoa sector, all from the private sector (seven from cocoa producing Member countries and seven from cocoa consuming Member countries). However, the Board, whose mandate is as extensive as that of the International Cocoa Council and comprises all aspects of the world cocoa economy, only functions in an advisory capacity, as all final decisions are taken by the International Cocoa Council. The Consultative Board was established in recognition of the importance of the private sector in the world cocoa economy and of the increasingly important role that trade and industry have been playing in ICCO.

International Sugar Agreement

The International Sugar Organization is an intergovernmental organization, based in London, which was established by the International Sugar Agreement of 1968, as the body responsible for administering the Agreement.[2] Unlike its predecessors under pre-1968 versions of the International Sugar Agreement, it does not have the power to regulate the international sugar trade by price-setting or export quotas but seeks to promote the trade in and consumption of sugar by gathering and publishing information on the sugar market, research into new uses for sugar and related products and as a forum for intergovernmental discussions on sugar.[1] As of May 2013, its membership consisted of the European Union and 61 other countries.

WORLD BANK

The World Bank is a vital source of financial and technical assistance to developing countries around the world. It helps governments in developing countries reduce poverty by providing them with money and technical expertise they need for a wide range of projects–such as education, health, infrastructure, communications, government reforms, and for many other purposes. More than 9,000 development professionals from more than 168 countries in the world work at the Bank, in more than 100 Countries. The term "World Bank" refers only to the International Bank for Reconstruction and Development (IBRD) and the International Development Association (IDA).

The term "World Bank Group" incorporates five closely associated entities that work collaboratively toward poverty reduction: the World Bank (IBRD and IDA), and three other agencies, the International Finance Corporation (IFC), the Multilateral Investment Guarantee Agency (MIGA), and the International Centre for Settlement of Investment Disputes (ICSID).

Members

The Bank is like a cooperative in which 188 member countries are shareholders. Under the Articles of Agreement

of the International Bank for Reconstruction and Development (IBRD), a country must first join the International Monetary Fund (IMF) prior to becoming a member of the Bank. Membership in IDA, IFC, and MIGA is conditioned upon membership in IBRD.

Organisation

These member countries, or shareholders, are represented by a Board of Governors, who are the ultimate policymakers at the World Bank. Generally, the governors are member countries' ministers of finance or ministers of development. They meet once a year at the Annual Meetings of the Boards of Governors of the World Bank Group and the International Monetary Fund.

The governors delegate specific duties to 25 Executive Directors, who work on-site at the Bank. The five largest shareholders, France, Germany, Japan, the United Kingdom and the United States appoint an executive director, while other member countries are represented by 20 elected executive directors.

The World Bank Group president chairs meetings of the Boards of Directors and is responsible for overall management of the Bank. The President is selected by the Board of Executive Directors for a five-year, renewable term. Jim Yong Kim is the 12th president of the Bank. He is chairman of the Bank's Board of Executive Directors and is also president of the five interrelated organizations that make up the World Bank Group. The president is selected by the Executive Directors for a five-year, renewable term. To learn more about the Bank's past presidents, go to the Archives.

Functioning of the world bank

The bank raises money in several different ways to support the low-interest and no-interest loans (credits) and grants that the World Bank (IBRD and IDA) offers to developing and poor countries. IBRD lending to developing countries is primarily financed by selling AAA-rated bonds in the world's financial markets. IBRD bonds are purchased by a wide range of private and institutional investors in North America, Europe, and Asia. While IBRD earns a small margin on this lending, the greater proportion of income comes from lending out our own capital. This capital consists of reserves built up over the years and money paid in from the bank's 188 member country shareholders. IBRD income also pays for World Bank operating expenses and has contributed to IDA and debt relief.

The bank also has US$178 billion in what is known as "callable capital," which could be drawn from shareholders as backing if needed to meet IBRD obligations for borrowings (bonds) or guarantees.

IDA, the world's largest source of interest-free loans and grant assistance to the poorest countries, is replenished every three years by 40 donor countries. Additional funds are regenerated through repayments of loan principal on 35-to-40-year, no-interest loans, which are then available for re-lending. IDA accounts for nearly 40 percent of our lending.

The bank often has a surplus at the end of the fiscal year, which is earned from the interest rates charged on some loans and from fees charged for its services. Some of the surplus goes to IDA–the part of the bank that provides grants and interest free loans to the world's poorest countries. The rest of the surplus is either used for debt relief for heavily indebted poor countries, added to financial reserves, or to respond to unforeseen humanitarian crises.

There is an independent panel called World Bank Inspection Panel to help ensure that operations adhere to operational policies and procedures.

Contributions of the World bank

During the past 40 years, life expectancy in developing countries has risen by 20 years–about as much as was achieved in all of human history prior to the mid-20th century. During the past 30 years, adult illiteracy in the developing world has been nearly halved to 25 percent. During the past 20 years, the absolute number of

people living on less than US$1 a day has begun to fall for the first time, even as the world's population has grown by 1.6 billion people. During the last decade, growth in the developing world has outpaced that in developed countries, helping to provide jobs and boost revenues poor countries' governments need to provide essential services.

India and the World Bank

With 1.2 billion people and the world's fourth largest economy, India's recent growth and development has been one of the most significant achievements. Over the six and half decades since independence, India has brought about a landmark agricultural revolution that has transformed the nation from chronic dependence on grain imports into a global agricultural powerhouse that is now a net exporter of food. Life expectancy has more than doubled, literacy rates have quadrupled, health conditions have improved, and a sizeable middle class has emerged. India is now home to globally- recognized companies in pharmaceuticals and steel and information and space technologies, and a growing voice on the international stage that is more in keeping with its enormous size and potential.

Historic changes are unfolding, unleashing a host of new opportunities to forge a 21st century nation. India will soon have the largest and youngest workforce the world has ever seen. At the same time, the country is in the midst of a massive wave of urbanization as some 10 million people move to towns and cities each year in search of jobs and opportunity - the largest rural-urban migration of this century.

Massive investments will be needed to create the jobs, housing, and infrastructure to meet soaring aspirations and make towns and cities more livable and green.

Inequity in all dimensions, including region, caste and gender, will need to be addressed. Poverty rates in India's poorest states are three to four times higher than those in the more advanced states. While India's average annual per capita income was $1,410 in 2011 - placing it among the poorest of the world's 'middle-income countries' - it was just $436 in Uttar Pradesh (which has more people than Brazil) and only $294 in Bihar, one of India's poorest states. Disadvantaged groups will need to be brought into the mainstream to reap the benefits of economic growth, and women – who "hold up half the sky" – empowered to take their rightful place in the socioeconomic fabric of the country.

Fostering greater levels of education and skills will be critical to promote prosperity in a rapidly globalizing world. However, while primary education has largely been universalized, learning outcomes remain low. Less than 10 percent of the working-age population has completed a secondary education, and too many secondary graduates do not have the knowledge and skills to compete in today's changing job market.

Improving healthcare will be equally important. Although India's health indicators have improved, maternal and child mortality rates remain very low and, in some states, are comparable to those in the world's poorest countries. Of particular concern is the nutrition of India's children whose well-being will determine the extent of India's much-awaited demographic dividend; at present, an overwhelming 40 percent (217 million) of the world's malnourished children are in India.

The country's infrastructure needs are massive. One in three rural people lack access to an all-weather road, and only one in five national highways is four-lane. Ports and airports have inadequate capacity, and trains move very slowly. An estimated 300 million people are not connected to the national electrical grid, and those who are face frequent disruptions. And, the manufacturing sector – vital for job creation - remains small and underdeveloped.

The new Country Partnership Strategy for India will guide the World Bank Group's support to India over the next five years (2013-2017). Developed in close consultation with the government and with inputs from civil society organizations and the private sector, the strategy aims to help India lay the foundations for achieving "faster, sustainable, and more inclusive growth" as outlined in the Government's 12th Five-Year Plan.

The World Bank Group supports India with an integrated package of financing, advisory services, and knowledge–one that is tailored to the needs of individual states. A key feature of the new strategy is the significant shift in support toward low-income and special category states, where many of India's poor and disadvantaged live.

This is also the World Bank Group's first country strategy to integrate the institution's new global goals for reducing poverty and increasing shared prosperity. It presents two scenarios that show India's potential for growth, poverty reduction and prosperity over the next 17 years. In the "2030 ambitious scenario" India grows on average at 8.2 percent, and makes economic growth as inclusive as its better-performing states during the latter part of the last decade. The potential is huge; poverty would be reduced from 29.8 percent (2010) to 5.5 percent by 2030 and the share of people no longer vulnerable to falling back into poverty would increase from 19.1 to 41.3 percent. If India were to grow as it did from 2005 to 2010 without making that growth more inclusive, poverty would fall to only 12.3 percent by 2030.

World Bank Group financing under the new strategy is expected to be $3 billion to $5 billion each year over the next five years. Sixty percent of the financing will go to state government-backed projects. Half of this, or 30 percent of total lending, will go to low-income or special category states.

Key focus areas

In the next five years, the World Bank Group will focus on three key areas of engagement: integration, rural-urban transformation, and inclusion. Common themes running across these areas will be improved governance, environmental sustainability, private sector, and gender equality.

- ***Integration*****:** India's massive infrastructure needs cannot be addressed through public investments alone. The strategy will accordingly focus on improving both public and private investments in infrastructure. For instance, the power sector, vital for economic growth, will need to build greater capacity and improve the reliability of generation, transmission and distribution. A vibrant manufacturing sector– especially small and medium size enterprises that are critical for the creation of jobs – will require the reform of labor laws, and improved access to land and finance. Better integration would result in more-balanced growth among Indian states, helping low-income states converge more quickly with their faster-growing neighbors.
- ***Rural-urban transformation*****:** 'Transformation' represents the biggest shift in the new strategy's approach. Well-managed urbanization can bring innumerable benefits to the 600 million people projected to live in India's cities by 2031. Accordingly, the new strategy aims to help India make the rural to urban shift as productive as possible in terms of growth and inclusion and improve the livability of urban areas, especially secondary cities where a sizeable population increase is taking place. At the same time, given agriculture's continued importance in the economic and social fabric of the country, the strategy will help India work toward raising agricultural productivity.
- ***Inclusion*****:** Economic integration and rural-urban transformation can benefit a large share of India's population only if there is a stronger focus on human development and on policies that help make growth inclusive. The World Bank Group will support the central and state governments in strengthening the nutrition policy as well as systems and capacities to improve nutrition. It will support government efforts to improve education mainly at the secondary and tertiary levels, with a more pronounced focus on quality across all levels of education. Special focus will be placed on ensuring access to education for underprivileged children, retaining girls in secondary education, and opening opportunities in higher education. It will also work to improve access to finance and to enhance social protection coverage for the more than 90% of the labor force that works in the informal sector.

The World Bank Group's past support to India's development agenda has contributed to improving outcomes in a range of sectors. Some results are highlighted below:

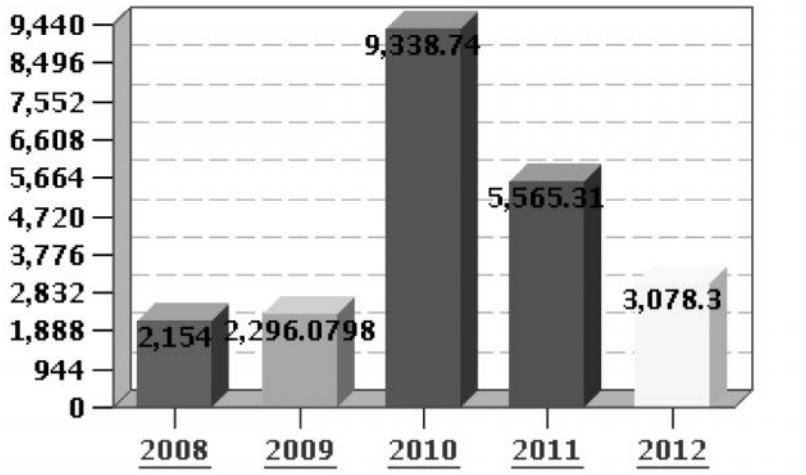
- Between 2001 and 2009, India's Education for All Program enrolled some 20 million out-of-school children, especially girls and children from socially disadvantaged families. By 2009, the number of out-of-school children had fallen to about 8.1 million. Over 98 percent of India's children now have access to a primary school within 1 kilometer of their home. The focus is now on improving the quality of learning, retaining children in school, and ensuring that more children are able to access and complete secondary education.
- World Bank support for vocational training programs in select institutions has helped more graduates to find jobs, with their numbers rising from just 32 percent in 2006 to over 60 percent in 2011. Nevertheless, empowering the large numbers of India's youth, especially in rural areas, with skills that are better matched with the demands of the labor market–whether informal or formal–will help them find jobs in the urban areas where better-paid work is more readily available.
- Rural livelihood programs have mobilized more than 30 million poor households in 90,000 villages to form 1.2 million self-help groups (SHGs) – up from 8 million in 2009. Ninety-five percent of SHG participants are women. In Andhra Pradesh alone, 10 million SHG women have seen their incomes rise by 115 percent. Members' savings exceeded $ 1.1 billion (2011) and access to credit rose by 200 percent to touch $5.8 billion (2000 -09). Support has also results in 30-40 percent higher prices for SHG products, tilting the terms of the trade in favor of poor people in India.
- Over past two decades, World Bank projects have contributed over $1.4 billion in financing for rural water supply and sanitation. About 24 million people in over 15,000 villages - with populations ranging from 150 to 15,000 – have benefited from these programs. In addition, some 17 million rural people have benefitted from improved sanitation.
- India has the largest burden of tuberculosis (TB) in the world. There are an estimated 2.2 million new TB cases in India every year, accounting for a quarter of the global burden. Between 1998 and 2012, two IDA credits totaling $279 million provided significant support to scale-up effective diagnosis and treatment under the national TB control program. During that period, over 15 million people with TB were diagnosed and treated by the program, saving an estimated 2.6 million lives. And, to date, the World Bank supported National AIDS program has reached about 81 percent of female sex workers, 66 percent of men having sex with men and 71 percent of injecting drug users, with targeted interventions. However, continued attention is needed to secure these gains.
- World Bank support for health projects has helped pregnant women to reach medical facilities in time for delivery; in Tamil Nadu, 99.5 percent of deliveries now take place in medical institutions. However, despite increasing rates of decline, maternal and child mortality rates remain on par with rates in much poorer countries. And while India has recorded impressive economic growth in the past decade, malnutrition rates has declined very little; in fact, stunting rates in India are two to seven times higher than those in other BRICS countries.
- From September 2004, World Bank support of some $2 billion is helping India's National Rural RoadsProgram to improve connectivity, especially in the economically weaker regions and hill states. Some 24,200 km of all-weather roads have benefitted rural people in the states of Himachal Pradesh, Jharkhand, Meghalaya, Punjab, Rajasthan, Uttarakhand and Uttar Pradesh. However, much more remains to be done; one-third of the rural population still lacks access to an all-weather road.
- Over the past decade or so, World Bank support for improving farmer incomes from rainfed lands in Karnataka, Himachal Pradesh and Uttarakhand have helped implement soil and water conservation measures and raise agricultural productivity. Lessons learnt have helped shape the Government of India's Common Watershed Guidelines and the design of national watershed programs.
- Since 1993, two Sodic Lands Reclamation Projects in Uttar Pradesh have brought more than 260,000 hectares of barren or unproductive lands under cultivation. Over 425,000 poor families have benefitted

from a three to six fold increase in crop yields. Around 15,000 SHGs have helped the women pool savings and connect to the formal banking network. In several villages, these SHGs now manage the mid-day meal provided in local state schools under a government program. A $197 million World Bank credit is now supporting the third phase of the project that aims to reclaim another 130,000 hectares of predominantly barren and low productivity sodic lands in about 25 districts of the state.

India Projects & Programs

The World Bank Group's Strategy for India for FY 2009 to FY 2012 is closely aligned with the country's objectives as outlined in its 11th Five Year Plan. The Bank uses lending and analytical work to help India achieve its goals. Between 2009 and 2012, the Bank lent around $19 billion to the country. As of March 2012, total net commitments stood at $23.4 billion (IBRD $15.6 billion, IDA 7.8 billion) across 75 projects.

India: Lending By Volume (Millions Of US Dollars)



INTERNATIONAL MONETARY FUND (IMF)

The International Monetary Fund (IMF) works to foster international monetary cooperation, secure financial stability, facilitate international trade, promote high employment and sustainable economic growth, and reduce poverty around the world. Created in 1945, the IMF is governed by and accountable to the 188 countries that make up its near-global membership.

The IMF, also known as the "Fund," was conceived at a United Nations conference convened in Bretton Woods, New Hampshire, United States, in July 1944. The 44 governments represented at that conference sought to build a framework for economic cooperation that would avoid a repetition of the vicious circle of competitive devaluations that had contributed to the Great Depression of the 1930s.

The IMF's responsibilities: The IMF's primary purpose is to ensure the stability of the international monetary system–the system of exchange rates and international payments that enables countries (and their citizens) to transact with one other. This system is essential for promoting sustainable economic growth, increasing living standards, and reducing poverty. The Fund's mandate has recently been clarified and updated to cover the full range of macroeconomic and financial sector issues that bear on global stability.

Fast Facts on the IMF

- *Membership*: 188 countries
- *Headquarters*: Washington, D.C.
- *Executive Board*: 24 Directors representing countries or groups of countries
- *Staff*: Approximately 2,503 from 144 countries
- *Total quotas*: US$360 billion (as of 3/14/13)
- *Additional pledged or committed resources*: US$1 trillion
- *Loans committed (as of 3/7/13)*: US$226 billion, of which US$166 billion have not been drawn (see table)
- *Biggest borrowers (amount agreed as of 3/7/13)*: Greece, Portugal, Ireland
- *Biggest precautionary loans (amount agreed as of 3/7/13)*: Mexico, Poland, Colombia
- *Surveillance consultations*: In 2011, 122 consultations were discussed and in 2012, 123 consultations were discussed
- *Technical assistance*: Field delivery in FY2012–246 person years
- *Transparency*: In 2012, about 91 percent of Article IV and program-related staff reports and policy papers were published (as of 3/20/2013)

Goals of IMF

Article I of the Articles of Agreement sets out the IMF's main goals:

- promoting international monetary cooperation;
- facilitating the expansion and balanced growth of international trade;
- promoting exchange stability;
- assisting in the establishment of a multilateral system of payments; and
- making resources available (with adequate safeguards) to members experiencing balance of payments difficulties.

Surveillance

To maintain stability and prevent crises in the international monetary system, the IMF reviews country policies, as well as national, regional, and global economic and financial developments through a formal system known as surveillance. Under the surveillance framework, the IMF provides advice to its 188 member countries, encouraging policies that foster economic stability, reduce vulnerability to economic and financial crises, and raise living standards. It provides regular assessment of global prospects in its World Economic Outlook, financial markets in its Global Financial Stability Report, and public finance developments in its Fiscal Monitor, and publishes a series of regional economic outlooks.

The key findings and policy advice from the various multilateral products, as well as the Managing Director's priorities are pulled together in the Global Policy Agenda. The Executive Board of the IMF adopted a new Decision on Bilateral and Multilateral Surveillance, also known as the Integrated Surveillance Decision. The decision provides guidance to the Fund and member countries on their roles and responsibilities in surveillance and took effect on January 18, 2013. More broadly, in response to the Triennial Surveillance Review completed in October 2011, efforts are underway to better integrate multilateral, financial, and bilateral surveillance, including

through: additional work on interconnections and spillovers; greater use of in-depth risk assessments; renewed emphasis on external stability–an External Sector Report now complements other surveillance; and strengthening the traction of IMF policy advice.

Financial assistance

IMF financing provides member countries the breathing room they need to correct balance of payments problems. A policy program supported by IMF financing is designed by the national authorities in close cooperation with the IMF, and continued financial support is conditioned on effective implementation of this program. In an early response to the recent global economic crisis, the IMF strengthened its lending capacity and approved a major overhaul of the mechanisms for providing financial support in April 2009, with further reforms adopted in August 2010 and December 2011.

In the most recent reforms, IMF lending instruments were improved further to provide flexible crisis prevention tools to a broad range of members with sound fundamentals, policies, and institutional policy frameworks. In low-income countries, the IMF doubled loan access limits and is boosting its lending to the world's poorer countries, supported by the windfall profits from gold sales, with interest rates set at zero through end-2014.

SDRs

The IMF issues an international reserve asset known as Special Drawing Rights (SDRs) that can supplement the official reserves of member countries. Two allocations in August and September 2009 increased the outstanding stock of SDRs almost ten-fold to total about SDR 204 billion (US$310 billion). Members can also voluntarily exchange SDRs for currencies among themselves. In a 2011 paper, IMF staff explore options to enhance the role of the SDR to promote stability of the international monetary system.

Technical assistance

The IMF provides technical assistance and training to help member countries strengthen their capacity to design and implement effective policies. Technical assistance is offered in several areas, including tax policy and administration, expenditure management, monetary and exchange rate policies, banking and financial system supervision and regulation, legislative frameworks, and statistics.

Resources

The IMF's resources are provided by its member countries, primarily through payment of quotas, which broadly reflect each country's economic size. At the April 2009 G-20 Summit, world leaders pledged to support a tripling of the IMF's lending resources from about US$250 billion to US$750 billion. To deliver on this pledge, the then current and new participants in the New Arrangements to Borrow (NAB) agreed to expand the NAB to about US$570 billion, which became effective on March 11, 2011 following completion of the ratification process by NAB participants. When concluding the 14th General Review of Quotas in December 2010, Governors agreed to double the IMF's quota resources to approximately US$730 billion and a major realignment of quota shares among members. When the quota increase becomes effective, there will be a corresponding rollback in NAB resources. In mid-2012, member countries announced additional pledges to increase the IMF's resources by $460 billion to help strengthen global economic and financial stability.

Historically, the annual expenses of running the Fund have been met mainly by interest receipts on outstanding loans, but the membership agreed in 2012 to adopt a new income model based on a range of revenue sources better suited to the diverse activities of the Fund.

Governance and organization

The IMF is accountable to the governments of its member countries. At the top of its organizational structure is

the Board of Governors, which consists of one Governor and one Alternate Governor from each member country. The Board of Governors meets once each year at the IMF-World Bank Annual Meetings. Twenty-four of the Governors sit on the International Monetary and Financial Committee (IMFC) and normally meet twice each year.

The day-to-day work of the IMF is overseen by its 24-member Executive Board, which represents the entire membership; this work is guided by the IMFC and supported by the IMF staff. In a package of reforms approved by the Governors in December 2010, the Articles of Agreement will be amended so as to facilitate a move to a more representative, all-elected Executive Board. The Managing Director is the head of the IMF staff and Chairman of the Executive Board, and is assisted by four Deputy Managing Directors.

India and the IMF

- India joined the IMF on December 27, 1945, as one of the IMF's original members.
- India accepted the obligations of Article VIII of the IMF Articles of Agreement on current account convertibility on August 20, 1994.
- India subscribes to the IMF's Special Data Dissemination Standard. Countries belonging to this group make a commitment to observe the standard and to provide information about their data and data dissemination practices.

Financial Assistance to India

While India has not been a frequent user of IMF resources, IMF credit has been instrumental in helping India respond to emerging balance of payments problems on two occasions. In 1981-82, India borrowed SDR 3.9 billion under an Extended Fund Facility, the largest arrangement in IMF history at the time. In 1991-93, India borrowed a total of SDR 2.2 billion under two stand-by arrangements, and in 1991 it borrowed SDR 1.4 billion under the Compensatory Financing Facility.

Technical Assistance to India

In recent years, the Fund has provided India with technical assistance in a number of areas, including the development of the government securities market, foreign exchange market reform, public expenditure management, tax and customs administration, and strengthening statistical systems in connection with the Special Data Dissemination Standards. Since 1981 the IMF Institute has provided training to Indian officials in national accounts, tax administration, balance of payments compilation, monetary policy, and other areas.

ASIAN DEVELOPMENT BANK

The Asian Development Bank aims for poverty free Asia and Pacific. Approximately 1.7 billion people in the region are poor and unable to access essential goods, services, assets and opportunities to which every human is entitled. Since its foundation in 1966, ADB has been driven by an inspiration and dedication to improving people's lives in Asia and the Pacific. ADB is committed to helping developing member countries evolve into modern economies that are well integrated with each other and the world through investment in infrastructure, health care services, financial and public administration systems, or helping nations prepare for the impact of climate change or better manage their natural resources. The main devices for assistance are loans, grants, policy dialogue, technical assistance and equity investments.

Key Facts	
President and Chairperson of the Board of Directors:	*Takehiko Nakao*
Members:	*67; 48 regional members; 19 nonregional members*
Offices:	*Headquarters in Manila, Philippines, with 28 resident missions and 3 representative offices in Tokyo, Frankfurt, and Washington, DC*
Founded:	*1966*
Budget:	*2013 Budget*
Financing in 2012:	*$21.57 billion*

Key achievements

- ADB aims for an Asia and Pacific free from poverty. While it has achieved a significant reduction in extreme poverty, the region remains home to about two-thirds of the world's extremely poor.
- With $21.57 billion in approved financing in 2012 and 3,045 employees from 61 of its 67 members, ADB in partnership with member governments, independent specialists and other financial institutions is focused on delivering projects that create economic and development impact.
- Environmental sustainability is a core strategy of ADB's work as it is the poor that are most severely affected. Environmental damage and resource depletion are already impeding the region's development and reducing the quality of life.
- ADB is active in creating the framework for the private sector to be involved in investing in new projects that underpin development and improve the lives of the 1.7 billion people in the region who live on less than $2 a day.
- Since 2000, the Asian Development Fund has transformed the region with the construction of thousands of schools, bridges, health clinics and roads, providing opportunities for people to lift themselves out of poverty.
- Over the past 6 years, ADB, through the Asian Development Fund has: expanded the access of more than 19 million students to quality education by building or upgrading more than 60,000 classrooms and training 720,000 teachers; helped more than 252 million people gain better access to wider economic opportunities and social services by building or upgrading more than 56,000 (km) of roads; provided more than 2.1 million households with access to clean ater by installing or rehabilitating about 14,000 km of water supply pipes; connected more than 1.8 million households to electricity by building or upgrading more than 35,000 km of power transmission and distribution lines; and reduced greenhouse gas emissions by 2 million tons of carbon dioxide equivalent per year by promoting more efficient and cleaner energy operations.

Members

Membership in the bank is open to members and associate members of the United Nations Economic and Social Commission for Asia and the Pacific; and other regional countries and non-regional developed countries that are members of the United Nations or of any of its specialized agencies. ADB was established with 31 members in 1966. Today ADB has grown to encompass 67 members - of which 48 are from within Asia and the Pacific and 19 outside.

Regional Members

Members	Year of Membership
Afghanistan	1966
Armenia	2005
Australia	1966
Azerbaijan	1999
Bangladesh	1973
Bhutan	1982
Brunei Darussalam	2006
Cambodia	1966
China, People's Republic of	1986
Cook Islands	1976
Fiji	1970
Georgia	2007
Hong Kong, China	1969
India	1966
Indonesia	1966
Japan	1966
Kazakhstan	1994
Kiribati	1974
Korea, Republic of	1966
Kyrgyz Republic	1994
Lao PDR	1966
Malaysia	1966
Maldives	1978
Marshall Islands	1990
Micronesia, Federated States of	1990
Mongolia	1991
Myanmar	1973
Nauru	1991
Nepal	1966
New Zealand	1966
Pakistan	1966
Palau	2003
Papua New Guinea	1971
Philippines	1966
Samoa	1966
Singapore	1966
Solomon Islands	1973
Sri Lanka	1966
Taipei,China	1966
Tajikistan	1998
Thailand	1966
Timor-Leste	2002
Tonga	1972
Turkmenistan	2000
Tuvalu	1993
Uzbekistan	1995
Vanuatu	1981
Viet Nam	1966
Nonregional Members	
Austria	1966
Belgium	1966
Canada	1966
Denmark	1966
Finland	1966
France	1970
Germany	1966
Ireland	2006
Italy	1966
Luxembourg	2003
The Netherlands	1966
Norway	1966
Portugal	2002
Spain	1986
Sweden	1966
Switzerland	1967
Turkey	1991
United Kingdom	1966
United States	1966

Board of Governors

Article 28 of the ADB Charter vests all the powers of the institution in the Board of Governors, which in turn delegates these powers to the Board of Directors, except for those powers reserved for the Board of Governors in the Charter. The Board of Governors meets formally once a year in ADB's Annual Meeting. P. Chidambaram is the chairman.

Board of Directors

The 12 members of the Board of Directors are elected by the Board of Governors. Eight of those 12 are elected by member countries from within the Asia Pacific region, and the four others are elected by member countries from outside the region. Each Director appoints an Alternate. The President of ADB chairs the Board of Directors. The Board of Directors performs its duties full time at the ADB headquarters in Manila, Philippines, and holds formal and executive sessions regularly. The Directors supervise ADB's financial statements, approve its administrative budget, and review and approve all policy documents and all loan, equity, and technical assistance operations

Management

The President is Chairperson of the Board of Directors, and under the Board's direction, conducts the business of ADB. He is responsible for the organization, appointment, and dismissal of the officers and staff in accordance with regulations adopted by the Board of Directors. The President is elected by the Board of Governors for a term of five years, and may be reelected. He is also the legal representative of ADB. The President heads a management team comprising six Vice-Presidents and the Managing Director General, who supervise the work of ADB's operational, administrative, and knowledge departments

Policies and Strategies

The Long-Term Strategic Framework of the Asian Development Bank 2008-2020 "Strategy 2020" identifies drivers of change that will be stressed in all its operations - developing the private sector, encouraging good governance, supporting gender equity, helping developing countries gain knowledge, and expanding partnerships with other development institutions, the private sector, and with community-based organizations. By 2012, 80% of ADB lending will be in five core operational areas, identified as comparative strengths of ADB:

- Infrastructure, including transport and communications, energy, water supply and sanitation and urban development
- Environment
- Regional cooperation and integration
- Finance sector development
- Education

ADB will continue to operate in health, agriculture, and disaster and emergency assistance, but on a more selective basis. ADB has developed a corporate results framework to assess its progress in implementing Strategy 2020. Annually, it will monitor implementation through the ADB Development Effectiveness Review.

History

ADB was conceived amid the postwar rehabilitation and reconstruction efforts of the early 1960s. The vision was of a financial institution that would be Asian in character and foster economic growth and cooperation in the region - then one of the poorest in the world. A resolution passed at the first Ministerial Conference on Asian Economic Cooperation held by the United Nations Economic Commission for Asia and the Far East in 1963 set that vision on the way to becoming reality. The Philippines capital of Manila was chosen to host the new institution

- the Asian Development Bank - which opened on 19 December 1966, with 31 members that came together to serve a predominantly agricultural region. Takeshi Watanabe was ADB's first President. For the rest of the 1960s, ADB focused much of its assistance on food production and rural development. Its operations included ADB's first technical assistance, loans, including a first on concessional terms in 1969, and bond issue in Germany.

ADB's assistance expanded in the 1970s into education and health, and then to infrastructure and industry. The gradual emergence of Asian economies in the latter part of the decade spurred demand for better infrastructure to support economic growth. ADB focused on improving roads and providing electricity. When the world suffered its first oil price shock, ADB shifted more of its assistance to support energy projects, especially those promoting the development of domestic energy sources in member countries. Cofinancing operations began to provide additional resources for ADB projects and programs. ADB first bond issue in Asia - worth $16.7 million and issued in Japan - took place in 1970. A major landmark was the establishment in 1974 of the Asian Development Fund to provide concessional lending to ADB's poorest members. At the close of the decade, some Asian economies had improved considerably and graduated from ADB's regular assistance. At the close of the decade, some Asian economies had improved considerably and graduated from ADB's regular assistance.

In the 1980s ADB made its first direct equity investment and began to use its track record to mobilize additional resources for development from the private sector. In the wake of the second oil crisis, ADB continued its support to infrastructure development, particularly energy projects. ADB also increased its support to social infrastructure, including gender, microfinance, environmental, education, urban planning, and health issues. In 1982, ADB opened its first field office - a Resident Mission in Bangladesh - to bring operations closer to their intended beneficiaries. Later in the decade, ADB approved a policy supporting collaboration with nongovernment organizations to address the basic needs of disadvantaged groups in its developing member countries.

In the 1990s ADB begin promoting regional cooperation, forging close ties among neighboring countries in the Greater Mekong Subregion. In 1995, ADB became the first multilateral organization to have a Board-approved governance policy to ensure that development assistance fully benefits the poor. Policies on the inspection function, involuntary resettlement, and indigenous peoples - designed to protect the rights of people affected by a project - were also approved. ADB's membership, meanwhile, continued to expand with the addition of several Central Asian countries following the end of the Cold War. In mid-1997, a severe financial crisis hit the region, setting back Asia's spectacular economic gains. ADB responded with projects and programs to strengthen financial sectors and create social safety nets for the poor. ADB approved its largest single loan-a $4 billion emergency loan to the Republic of Korea-and established the Asian Currency Crisis Support Facility to accelerate assistance. In 1999, recognizing that development was still bypassing so many in the region, ADB adopted poverty reduction as its overarching goal.

In 2003, a severe acute respiratory syndrome (SARS) epidemic hit the region, making it clear that fighting infectious diseases requires regional cooperation. ADB began providing support at national and regional levels to help countries more effectively respond to avian influenza and the growing threat of HIV/AIDS. ADB also had to respond to unprecedented natural disasters, committing more than $850 million for recovery in areas of India, Indonesia, Maldives, and Sri Lanka hit by the December 2004 Asian tsunami. In addition, a $1 billion line of assistance to help victims of the October 2005 earthquake in Pakistan was set up. In 2008, ADB's Board of Directors approved Strategy 2020: The Long-Term Strategic Framework of the Asian Development Bank 2008-2020, a policy document guiding its operations to 2020. In 2009, ADB's Board of Governors agreed to triple ADB's capital base from $55 billion to $165 billion, giving it much-needed resources to respond to the global economic crisis. The 200% increase is the largest in ADB's history, and the first since the 1994 100% capital increase.

Working of ADB

– ADB raises funds through bond issues on the world's capital markets. We also rely on our members' contributions, retained earnings from our lending operations, and the repayment of loans.

- It provides loans and grants from a number of Special Funds. The largest is the Asian Development Fund, which offers grants and loans at very low interest rates.
- ADB's highest policy-making body is the Board of Governors, which meets annually and comprises one representative from each member nation – 48 from the Asia-Pacific and 19 from outside the region. The Governors elect 12 members of the Board of Directors. The ADB President, assisted by six Vice Presidents and a Managing Director General, manages the business of ADB.
- ADB consults people from all sections of society to ensure that projects, programs, and strategies meet people's needs. The country partnership strategy - the main planning document at the country level - emphasizes consultation with the government, the private sector, civil society, and all project stakeholders.

India and ADB

India has been a founding member of the Asian Development Bank (ADB) since its establishment in 1966. Since the beginning of its lending operations in the country in 1986, ADB has partnered with India in its endeavor to reduce poverty through infrastructure-led growth. Over the years, ADB has aligned its India program with the government's increasing focus on inclusive and sustainable growth. While continuing its support for infrastructure development in the energy, transport, and urban sectors, ADB is also now engaged in improving water resources management, agribusiness infrastructure development, promoting financial inclusion, and skills development. In line with the government's Finance Plus approach, ADB has been infusing innovations and regional best practices into project design and implementation. ADB has focused on strengthening its partnership with multilateral and bilateral development partners in India. In 2012, consultations and programming-related meetings were held with several key partners. Such consultations help ADB in being more responsive to development needs besides being useful in identifying strategies and approaches that add value to its overall program in India. ADB's partnerships with civil society organizations aim to strengthen the effectiveness, quality, and sustainability of development efforts. Civil society organizations partnering in ADB operations provide a grassroots perspective on the design and implementation of projects, assist in community mobilization and resettlement, provide technical training, and conduct independent monitoring and evaluation.

***Operational Challenges*:** Rapid economic growth in India over the past 2 decades has lifted millions out of poverty. However, income disparities and regional imbalances remain. To supplement the government's efforts in reducing interstate disparities and promoting regionally balanced growth, ADB has expanded its operations in low income and special category states. These states face one or more of the following constraints–high poverty, low incomes, low levels of social development, weak capacity, and inadequate infrastructure. From 2009 to 2012, between 60% to 80% of ADB's project approvals involved such states. An important aspect of ADB's engagement in these states has been its support to strengthening the capacities of executing agencies in planning and implementation of infrastructure projects, and exposing them to new technologies and international and regional best practices. The Capacity Development Resource Center at ADB's India Resident Mission is playing a key role in institutionalizing support to executing agencies. It has strengthened its ties with national training institutes and is committed to becoming a focal point for capacity building and knowledge solutions in the infrastructure domain. In tandem, enhanced tripartite review meetings involving ADB, the Government of India, and executing agencies are helping to not only minimize delays in project implementation, but also improve readiness and innovativeness of projects in the pipeline.

***Future Directions*:** ADB will continue to support the strategic goals of the government–faster, more inclusive, and sustainable growth– as emphasized in the 12th Five-Year Plan and reflected in ADB's country partnership strategy (CPS), 2013–2017 for India, currently being formulated. The strategic pillars of the new CPS will emphasize three agendas: support for inclusive growth, environmentally sustainable growth, and regional integration. Continued support to the development efforts of low-income and special category states will remain a key plank of operations over the new CPS period. Concurrently, operations will be designed around selected flagship operations that support the development of high-priority economic corridors, create markets for infrastructure

finance, and promote regional cooperation and integration through the South Asia Sub-regional Economic Cooperation (SASEC) platform. The 3-year lending program over 2013–2015 will average around $2 billion annually in terms of sovereign operations. The funds will be allocated across four core infrastructure sectors–transport, energy, urban, and agriculture and natural resources– and two cross-cutting sectors–finance and skills development. ADB's private sector operations will continue to support ADB's strategic priorities in these areas.

India is ADB's fourth largest shareholder. Since launching its lending operations in India in 1986, ADB has approved 168 sovereign loans amounting to $27.2 billion. As of 31 December 2012, the portfolio included 78 ongoing sovereign loans amounting to $11.2 billion. ADB's sovereign lending assistance to India increased from an annual average of about $1.16 billion in 2000–2006 to $1.85 billion in 2007–2012. India has been ADB's largest borrower for the last 3 years (2010–2012).

ADB-Supported Projects and Programs ADB-supported projects and programs have had significant development impacts and worked toward improving the lives of the ultimate beneficiaries in following ways:

- The Madhya Pradesh State Roads II (2007–2011) project facilitated construction and rehabilitation of approximately 1,800 kilometers (km) of state roads, thereby improving access to business opportunities and social services, particularly benefiting small business owners and farmers. ADB-supported initiatives in the energy sector are helping India scale up access to electricity through projects like the Assam Power Sector Enhancement Investment Project (2009– 2014). The financing facility will strengthen the transmission and distribution system and is expected to benefit around 1 million households, businesses, hospitals, and schools through increased access to power.
- ADB-assisted Chhattisgarh Irrigation Development Project (2005–2013) is supporting a participatory irrigation management approach to rehabilitate and upgrade irrigation infrastructure to improve water resource management, helping increase productivity of irrigated agriculture and enhancing livelihoods in the state. More than 150,000 farmers will benefit.
- Meanwhile, the Kolkata Environmental Improvement Project (2000–2012) has improved overall living and environmental conditions for nearly 1.4 million inhabitants through the construction of 331 km of sewage and drainage networks. Recent projects and programs include an innovative partial credit guarantee facility that will support credit enhancements of infrastructure project bonds to enable cash-rich pension funds and insurers to invest in such bonds (India Infrastructure Finance Company Limited–Credit Enhancement of Project Bonds); and assistance to West Bengal for stabilizing its fiscal situation and encouraging reforms of administrative processes to promote efficient public spending and improvements in revenue collection (West Bengal Development Finance Program).

Co-financing operations enable ADB's financing partners, governments or their agencies, multilateral financing institutions, and commercial organizations, to participate in the financing of ADB projects. The additional funds are provided in the form of official loans and grants, and commercial financing, such as B loans, risk transfer arrangements, parallel loans, and co-financing for transactions under ADB's Trade Finance Program. By the end of 2012, cumulative direct value-added official co-financing for India amounted to $1.09 billion for 17 investment projects, and $87.8 million for 105 technical assistance projects. In 2012, India received $200 million loan co-financing from the Government of Germany for Himachal Pradesh Clean Energy Development Investment Program–Tranche 4, and $2.5 million grant co-financing from the Japan Fund for Poverty Reduction for Livelihood Improvement for River Erosion Victims in Assam.

As a catalyst for private investments, ADB provides direct financial assistance to non sovereign public sector and private sector projects in the form of direct loans, equity investments, guarantees, B loans, and trade finance. Since its inception, ADB has approved a total of $3,338.3 million in non sovereign financing for India, $2,060.3 million of which were for 38 private sector projects. Total outstanding balances and commitments of ADB's non sovereign transactions in the country as of 31 December 2012 totalled $1,722.1 million, representing 23.5% of ADB's total non sovereign portfolio.

Procurement: From 1 January 1966 to 31 December 2012, contractors and suppliers were involved in 185,090 contracts for ADB loan projects worth $116.58 billion. During the same period, contractors and suppliers from India were involved in 7,973 contracts for ADB loan projects worth $14.74 billion. From 1 January 1966 to 31 December 2012, consultants were involved in 11,990 contracts for ADB loan projects worth $5.11 billion. During the same period, consultants from India were involved in 383 contracts for ADB loan projects worth $345.99 million. From 1 January 1966 to 31 December 2012, consultants were involved in 26,546 contracts for ADB technical assistance projects worth $3.1 billion. During the same period, consultants from India were involved in 1,673 contracts for ADB technical assistance projects worth $144.20 million.

LESSON ROUND UP

- The World Trade Organization (WTO) deals with the rules of trade between nations at a global or near-global level. It's an organization for liberalizing trade.
- It's a forum for governments to negotiate trade agreements. It's a place for them to settle trade disputes.
- MFN means that every time a country lowers a trade barrier or opens up a market, it has to do so for the same goods or ser-vices from all its trading partners – whether rich or poor, weak or strong.
- The principle of national treatment states that imported and locally-produced goods should be treated equally, at least after the foreign goods has entered the market.
- Dispute settlement is the central pillar of the multilateral trading system. Without a means of settling disputes, the rules-based system would be less effective because the rules could not be enforced.
- Settling disputes is the responsibility of the Dispute Settlement Body (the General Council), which consists of all WTO members.
- The Dispute Settlement Body has the sole authority to establish "panels" of experts to consider the case, and to accept or reject the panels' findings or the results of an appeal.
- The WTO has 153 members, accounting for over 97% of world trade.
- All WTO members may participate in all councils, committees, etc, except Appellate Body, Dispute Settlement panels, Textiles Monitoring Body, and plurilateral committees.
- The WTO Secretariat, based in Geneva, has around 625 staff and is headed by a director general. It does not have branch offices outside Geneva.
- The WTO agreements cover goods, services and intellectual property. They spell out the principles of liberalization, and the permitted exceptions.
- UNCTAD was established in 1964 to promote the development-friendly integration of developing countries into the world economy. 194 countries are member of UNCTAD.
- The highest decision-making body of UNCTAD is the quadrennial conference, at which member States make assessments of current trade and development issues, discuss policy options and formulate global policy responses.
- International commodity agreement is an agreement among producing and consuming countries to improve the functioning of the global market for a commodity.
- International Commodity Agreements are overseen by UNCTAD. In its Final Act, the UNCTAD-I made a comprehensive statement on the functions of International Commodity Agreements.
- The World Bank is a vital source of financial and technical assistance to developing countries around the world.

- It helps governments in developing countries reduce poverty by providing them with money and technical expertise they need for a wide range of projects–such as education, health, infrastructure, communications, government reforms, and for many other purposes.
- More than 9,000 development professionals from more than 168 countries in the world work at the Bank, in more than 100 Countries.
- The Bank is like a cooperative in which 188 member countries are shareholders.
- The bank raises money in several different ways to support the low-interest and no-interest loans (credits) and grants that the World Bank (IBRD and IDA) offers to developing and poor countries. IBRD lending to developing countries is primarily financed by selling AAA-rated bonds in the world's financial markets.
- The International Monetary Fund (IMF) works to foster international monetary cooperation, secure financial stability, facilitate international trade, promote high employment and sustainable economic growth, and reduce poverty around the world.
- The IMF is governed by and accountable to the 188 countries that make up its near-global membership.
- The IMF's primary purpose is to ensure the stability of the international monetary system – the system of exchange rates and international payments that enables countries (and their citizens) to transact with one other.
- IMF financing provides member countries the breathing room they need to correct balance of payments problems.
- The IMF issues an international reserve asset known as Special Drawing Rights (SDRs) that can supplement the official reserves of member countries.
- The IMF provides technical assistance and training to help member countries strengthen their capacity to design and implement effective policies.
- The IMF's resources are provided by its member countries, primarily through payment of quotas, which broadly reflect each country's economic size.
- The Asian Development Bank aims for poverty free Asia and Pacific. Approximately 1.7 billion people in the region are poor and unable to access essential goods, services, assets and opportunities to which every human is entitled.
- ADB aims for an Asia and Pacific free from poverty. While it has achieved a significant reduction in extreme poverty, the region remains home to about two-thirds of the world's extremely poor.
- ADB has grown to encompass 67 members - of which 48 are from within Asia and the Pacific and 19 outside.
- ADB raises funds through bond issues on the world's capital markets. We also rely on our members' contributions, retained earnings from our lending operations, and the repayment of loans.
- It provides loans and grants from a number of Special Funds. The largest is the Asian Development Fund, which offers grants and loans at very low interest rates.

SELF TEST QUESTIONS

1. Explain the principles of WTO which are foundation of multilateral trading system.
2. Give a critical note on the Uruguay Round.
3. What are the differences between GATT and WTO

4. Explain the dispute settlement process of WTO.
5. Write a note on following agreements of WTO
   (a) Agreement on Non tariff barriers.
   (b) Agreement on Agriculture
   (c) TRIPS
   (d) TRIMS
   (e) GATS
6. What is the role of UNCTAD in promotion of international trade?
7. What are international commodity agreements? Give some examples of international commodity agreements prevalent in the trading world.
8. Discuss the functions and role of World Bank.
9. Evaluate World Bank assistance to India.
10. Discuss the functions and role of IMF.
11. Give a brief account on ADB's policies and assistance in respect of developing countries.
12. Write a short note on importance and functioning of ADB.

Lesson 8
Anti Dumping Duties

LESSON OUTLINE

- Dumping
- Anti-dumping
- Difference between Anti-Dumping Duty & Normal Customs Duty
- WTO Provisions on Anti-Dumping
- Anti-Dumping Agreement
- Regulatory framework for anti-dumping in India
- Institutional arrangement in India for anti-dumping
- Anti-Dumping Duties- Procedures in India
- Recent Anti Dumping Cases in India
- Case Study
- LESSON ROUND UP
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

In economics, "dumping" is a kind of predatory pricing, especially in the context of international trade. Dumping is the act of charging a lower price for the like goods in a foreign market than one charges for the same good in a domestic market for consumption in the home market of the exporter. Under the World Trade Organization (WTO) Agreement, dumping is condemned (but is not prohibited) if it causes or threatens to cause material injury to a domestic industry in the importing country.

The term has a negative connotation, as advocates of competitive markets see "dumping" as a form of protectionism. The logic behind anti-dumping duties is to save domestic jobs, although critics argue that this leads to higher prices for domestic consumers and reduces the competitiveness of domestic companies producing similar goods.

With the increase in international trade there has been significant increase in anti dumping duties levied by all countries.

In this chapter we examine the provisions of WTO on Anti Dumping and procedures of anti dumping in India.

If the other fellow sells cheaper than you, it is called dumping. 'Course, if you sell cheaper than him, that's mass production.

Will Rogers

DUMPING

Dumping is said to occur when goods are exported by one country to another country at a price lower than **the normal value of the goods**. This is an unfair trade practice which can have a distortive effect on international trade. Often, dumping is mistaken and simplified to mean cheap or low priced imports. However, it is a misunderstanding of the term. Dumping implies low priced imports only in the relative sense (relative to the normal value) and not in absolute sense. Imports of cheap products through illegal trade channels like smuggling do not fall within the purview of anti-dumping measures.

ANTI DUMPING

Anti dumping is a measure to rectify the situation arising out of the dumping of goods and its trade distortive effect. Thus, the purpose of anti dumping duty is to rectify the trade distortive effect of dumping and re-establish fair trade. The use of anti dumping measure as an instrument of fair competition is permitted by the WTO. In fact, anti dumping is an instrument for ensuring fair trade and is not a measure of protection per se for the domestic industry. It provides relief to the domestic industry against the injury caused by dumping. In fact, anti dumping is a trade remedial measure to counteract the trade distortion caused by dumping and the consequential injury to the domestic industry. Only in this sense, it can be seen as a protective measure. It can never be regarded as a protectionist measure.

DIFFERENCE BETWEEN ANTI DUMPING DUTY AND NORMAL CUSTOMS DUTY

Although anti dumping duty is levied and collected by the Customs Authorities, it is entirely different from the Customs duties not only in concept and substance, but also in purpose and operation. The following are the main differences between the two: -

- Conceptually, anti dumping and the like measures in their essence are linked to the notion of fair trade. The object of these duties is to guard against the situation arising out of unfair trade practices while customs duties are there as a means of raising revenue and for overall development of the economy.
- Customs duties fall in the realm of trade and fiscal policies of the Government while anti dumping and anti subsidy measures are there as trade remedial measures.
- The object of anti dumping and allied duties is to offset the injurious effect of international price discrimination while customs duties have implications for the government revenue and for overall development of the economy.
- Anti dumping duties are not necessarily in the nature of a tax measure inasmuch as the Authority is empowered to suspend these duties in case of an exporter offering a price undertaking. Thus such measures are not always in the form of duties/tax.
- Anti dumping and anti subsidy duties are levied against exporter / country inasmuch as they are country specific and exporter specific as against the customs duties which are general and universally applicable to all imports irrespective of the country of origin and the exporter.

Thus, there are basic conceptual and operational differences between the customs duty and the anti dumping duty. The anti dumping duty is levied over and above the normal customs duty chargeable on the import of goods in consideration.

WTO – PROVISIONS ON ANTI DUMPING

If a company exports a product at a price lower than the price it normally charges on its own home market, it is said to be “dumping” the product. Many governments treat this as unfair competition and take action against

dumping in order to defend their domestic industries. The WTO agreement does not pass judgement. Its focus is on how governments can or cannot react to dumping. It disciplines anti-dumping actions.

GATT (Article 6) allows countries to take action against dumping. The Anti-Dumping Agreement clarifies and expands Article 6, and the two operate together. They allow countries to act in a way that would normally break the GATT principles of not discriminating between trading partners. Typically anti-dumping action means charging extra import duty on the particular product from the particular exporting country in order to bring its price closer to the "normal value" or to remove the injury to domestic industry in the importing country. The governments can take actions against dumping where there is genuine ("material") injury to the competing domestic industry. In order to do that the government has to show that dumping is taking place, calculate the extent of dumping (how much lower the export price is compared to the exporter's home market price), and show that the dumping is causing injury or threatening to do so.

There are many different ways of calculating whether a particular product is being dumped heavily or only lightly. The agreement narrows down the range of possible options. It provides three methods to calculate a product's "normal value". The main one is based on the price in the exporter's domestic market. When this cannot be used, two alternatives are available — the price charged by the exporter in another country, or a calculation based on the combination of the exporter's production costs, other expenses and normal profit margins. And the agreement also specifies how a fair comparison can be made between the export price and what would be a normal price.

Calculating the extent of dumping on a product is not enough. Anti-dumping measures can only be applied if the dumping is hurting the industry in the importing country. Therefore, a detailed investigation has to be conducted according to specified rules first. The investigation must evaluate all relevant economic factors that have a bearing on the state of the industry in question. If the investigation shows dumping is taking place and domestic industry is being hurt, the exporting company can undertake to raise its price to an agreed level in order to avoid anti-dumping import duty.

Detailed procedures are set out on how anti-dumping cases are to be initiated, how the investigations are to be conducted, and the conditions for ensuring that all interested parties are given an opportunity to present evidence. Anti-dumping measures must expire five years after the date of imposition, unless an investigation shows that ending the measure would lead to injury.

Anti-dumping investigations are to end immediately in cases where the authorities determine that the margin of dumping is insignificantly small (defined as less than 2% of the export price of the product). Other conditions are also set. For example, the investigations also have to end if the volume of dumped imports is negligible (i.e. if the volume from one country is less than 3% of total imports of that product — although investigations can proceed if several countries, each supplying less than 3% of the imports, together account for 7% or more of total imports).

The agreement says member countries must inform the Committee on Anti-Dumping Practices about all preliminary and final anti-dumping actions, promptly and in detail. They must also report on all investigations twice a year. When differences arise, members are encouraged to consult each other. They can also use the WTO's dispute settlement procedure.

Article VI of GATT and the Anti-Dumping Agreement

The GATT 1994 sets forth a number of basic principles applicable in trade between Members of the WTO, including the "most favoured nation" principle. It also requires that imported products not be subject to internal taxes or other changes in excess of those imposed on domestic goods, and that imported goods in other respects be accorded treatment no less favourable than domestic goods under domestic laws and regulations, and establishes rules regarding quantitative restrictions, fees and formalities related to importation, and customs valuation. Members of the WTO also agreed to the establishment of schedules of bound tariff rates. Article VI of

GATT 1994, on the other hand, explicitly authorizes the imposition of a specific anti-dumping duty on imports from a particular source, in excess of bound rates, in cases where dumping causes or threatens injury to a domestic industry, or materially retards the establishment of a domestic industry.

The Agreement on Implementation of Article VI of GATT 1994, commonly known as the Anti-Dumping Agreement, provides further elaboration on the basic principles set forth in Article VI itself, to govern the investigation, determination, and application, of anti-dumping duties.

ANTI-DUMPING AGREEMENT

The original GATT agreement encouraged lower tariff rates for promotion of trade among countries which over time led to imposition of increasing anti dumping duties. The Article VI of the GATT to govern the imposition of anti dumping duties became more apparent. The Article VI contains various provisions for its regulation but was not exhaustive. For example: it requires a determination of material injury, but does not contain any guidance as to criteria for determining whether such injury exists, and addresses the methodology for establishing the existence of dumping in only the most general fashion. Consequently, contracting parties to GATT negotiated more detailed Codes relating to anti-dumping. The first such Code, the Agreement on Anti-Dumping Practices, entered into force in 1967 as a result of the Kennedy Round. However, the United States never signed the Kennedy Round Code, and as a result the Code had little practical significance.

The Tokyo Round Code, which entered into force in 1980, represented a quantum leap forward. Substantively, it provided enormously more guidance about the determination of dumping and of injury than did Article VI. Equally important, it set out in substantial detail certain procedural and due process requirements that must be fulfilled in the conduct of investigations. Nevertheless, the Code still represented no more than a general framework for countries to follow in conducting investigations and imposing duties.

Negotiations in the Uruguay Round have resulted in a revision of this Agreement which addresses many areas in which the current Agreement lacks precision and detail. Article VI of GATT 1994 explicitly authorizes the imposition of a specific anti-dumping duty on imports from a particular source, in excess of bound rates, in cases where dumping causes or threatens injury to a domestic industry, or materially retards the establishment of a domestic industry.

The Agreement on Implementation of Article VI of GATT 1994 is commonly known as the Anti-Dumping Agreement (or the AD Agreement). It provides detailed rules in relation to the method of determining that a product is dumped, the criteria to be taken into account in a determination that dumped imports cause injury to a domestic industry, the procedures to be followed in initiating and conducting anti-dumping investigations, and the implementation and duration of anti-dumping measures. In addition, the new agreement clarifies the role of dispute settlement panels in disputes relating to anti-dumping actions taken by domestic authorities.

Basic principles of the Anti Dumping Agreement

Article 1 of the Agreement establishes the basic principle that WTO Members can impose anti-dumping measures, if, after investigation in accordance with the Agreement, a determination is made:

(a) that dumping is occurring,

(b) that the domestic industry producing the like product in the importing country is suffering material injury, and

(c) that there is a causal link between the two.

Committee on Anti-Dumping Practices

The Committee meets at least twice a year. It provides Members of the WTO the opportunity to discuss any

matters relating to the Anti-Dumping Agreement (Article 16). The Committee has undertaken the review of national legislations notified to the WTO. This offers the opportunity to raise questions concerning the operation of national anti-dumping laws and regulations, and also questions concerning the consistency of national practice with the Anti-Dumping Agreement. The Committee also reviews notifications of anti-dumping actions taken by Members, providing the opportunity to discuss issues raised regarding particular cases.

The Committee has created a separate body, the Ad Hoc Group on Implementation, which is open to all Members of the WTO, and which is expected to focus on technical issues of implementation: that is, the "how to" questions that frequently arise in the administration of anti-dumping laws.

Dispute settlement

Disputes in the anti-dumping area are subject to binding dispute settlement before the Dispute Settlement Body of the WTO, in accordance with the provisions of the Dispute Settlement Understanding ("DSU") (Article 17). Members may challenge the imposition of anti-dumping measures, in some cases may challenge the imposition of preliminary anti-dumping measures, and can raise all issues of compliance with the requirements of the Agreement, before a panel established under the DSU. In disputes under the Anti-Dumping Agreement, a special standard of review is applicable to a panel's review of the determination of the national authorities imposing the measure. The standard provides for a certain amount of deference to national authorities in their establishment of facts and interpretation of law, and is intended to prevent dispute settlement panels from making decisions based purely on their own views. The standard of review is only for anti-dumping disputes, and a Ministerial Decision provides that it shall be reviewed after three years to determine whether it is capable of general application.

Notifications

All WTO Members are required to bring their anti-dumping legislation into conformity with the Anti-Dumping Agreement, and to notify that legislation to the Committee on Anti-Dumping Practices. While the Committee does not "approve" or "disapprove" any Members' legislation, the legislations are reviewed in the Committee, with questions posed by Members, and discussions about the consistency of a particular Member's implementation in national legislation of the requirements of the Agreement.

In addition, Members are required to notify the Committee twice a year about all anti-dumping investigations, measures, and actions taken. The Committee has adopted a standard format for these notifications, which are subject to review in the Committee.

Finally, Members are required to promptly notify the Committee of preliminary and final anti-dumping actions taken, including in their notification certain minimum information required by Guidelines agreed to by the Committee. These notifications are also subject to review in the Committee

Dumping

Dumping is, in general, a situation of international price discrimination, where the price of a product when sold in the importing country is less than the price of that product in the market of the exporting country. Thus, in the simplest of cases, one identifies dumping simply by comparing prices in two markets. The determinations of appropriate price in the market of the exporting country (known as the "normal value") and the appropriate price in the market of the importing country (known as the "export price") is done following certain rules which are discussed below.

DETERMINATION OF NORMAL VALUE

General rule

The normal value is generally the price of the product at issue, in the ordinary course of trade, when destined for consumption in the exporting country market. In certain circumstances, for example when there are no sales in the domestic market, it may not be possible to determine normal value on this basis. The Agreement provides alternative methods for the determination of normal value in such cases.

Sales in the ordinary course of trade

One of the most complicated questions in anti-dumping investigations is the determination whether sales in the exporting country market are made in the "ordinary course of trade" or not. One of the bases on which countries may determine that sales are not made in the ordinary course of trade is if sales in the domestic market of the exporter are made below cost. The Agreement defines the specific circumstances in which home market sales at prices below the cost of production may be considered as not made in theordinary course of trade", and thus may be disregarded in the determination of normal value (Article 2). Those sales must be made at prices that are below per unit fixed and variable costs plus administrative, selling and general costs, they must be made within an extended period of time (normally one year, but in no case less than six months), and they must be made in substantial quantities. Sales are made in substantial quantities when (a) the weighted average selling price is below the weighted average cost; of (b) 20% of the sales by volume were below cost. Finally, sales made below costs may only be disregarded in the determination of normal value where they do not allow for recovery of costs within a reasonable period of time. If sales are below cost when made but are above the weighted average cost over the period of the investigation, the Agreement provides that they allow for recovery of costs within a reasonable period of time.

Insufficient volume of sales

If there are sales below cost that meet the criteria set out in the Agreement, they can simply be ignored in the calculation of normal value, and normal value will be determined based on the remaining sales. However, exclusion of these below-cost sales may result in a level of sales insufficient to determine normal value based on home market prices. It is obvious that, in the case where there are no sales in the exporting country of the product under investigation, it is not possible to base normal value on such sales, and the Agreement recognizes this. However, it is also possible that, while there are some sales in the exporting country's market, the level of such sales is so low that its significance is questionable. Thus, the Agreement recognizes that in some cases sales in the home market may be so low in volume that they do not permit a proper comparison of home market and export prices. It provides that the level of home market sales is sufficient if home market sales constitute 5 per cent or more of the export sales in the country conducting the investigation, provided that a lower ratio "should" be accepted if the volume of domestic sales nevertheless is "of sufficient magnitude" to provide for a fair comparison.

Alternative bases for calculating normal value

Two alternatives are provided for the determination of normal value if sales in the exporting country market are not an appropriate basis. These are (a) the price at which the product is sold to a third country; and (b) the "constructed value" of the product, which is calculated on the basis of the cost of production, plus selling, general, and administrative expenses, and profits. The Agreement contains detailed and specific rules for the determination of a constructed value, governing the information to be used in determining the amounts for costs, expenses, and profits, the allocation of these elements of constructed value to the specific product in question, and adjustments for particular situations such as start-up costs and non-recurring cost items.

Constructed normal value

The determination of normal value based on cost of production, selling, general and administrative expenses, and profits is referred to as the “constructed normal value” The rules for determining whether sales are made below cost also apply to performing a constructed normal value calculation. The principal difference is the inclusion of a “reasonable amount for profits” in the constructed value.

Third country price as normal value

The other alternative method for determining normal value is to look at the comparable price of the like product when exported to an appropriate third country, provided that price is representative. The Agreement does not specify any criteria for determining what third country is appropriate.

Indirect exports

In the situation where products are not imported directly from the country of manufacture, but are exported from an intermediate country, the Agreement provides that the normal value shall be determined on the basis of sales in the market of the exporting country. However, the Agreement recognizes that this may result in an inappropriate or impossible comparison, for instance if the product is not produced in the exporting country, there is no comparable price for the product in the exporting country, or the product is merely transshipped through the exporting country. In such cases, the normal value may be determined on the basis of the price of the product in the country of origin, and not the price in the exporting country.

Non-market economies

In the particular situation of economies where the government has a complete or substantially complete monopoly of its trade and where all domestic prices are fixed by the State, GATT 1994 and the Agreement recognize that a strict comparison with home market prices may not be appropriate. Importing countries have thus exercised significant discretion in the calculation of normal value of products exported from non-market economies.

DETERMINATION OF EXPORT PRICE

General rule

The export price will normally be based on the transaction price at which the foreign producer sells the product to an importer in the importing country. However, as is the case with normal value, the Agreement recognizes that this transaction price may not be appropriate for purposes of comparison.

Exceptions

There may be no export price for a given product, for instance, if the export transaction is an internal transfer, or if the product is exchanged in a barter transaction. In addition, the transaction price at which the exporter sells the product to the importing country may be unreliable because of an association or a compensatory arrangement between the exporter and the importer or a third party. In such a case, the transaction price may not be an arms-length market price, but may be manipulated, for instance for tax purposes. The Agreement recognizes that, in such cases, an alternative method of determining an appropriate export price for comparison is needed.

Alternative method of calculation

The Agreement provides that in circumstances where there is no export price, or where the export price is unreliable due to an association or compensatory arrangement between the exporter and the importer or a third party, an alternative method may be used to determine the export price. this results in a “constructed export price”, and is calculated on the basis of the price at which the imported products are first resold in an independent

buyer. If the imported product is not resold to an independent buyer, or is not resold as imported, the authorities may determine a reasonable basis on which to calculate the export price.

FAIR COMPARISON OF NORMAL VALUE AND EXPORT PRICE

Basic requirements

The Agreement requires that a fair comparison of the export price and the normal value be made. The basic requirements for a fair comparison are that the prices being compared are those of sales made at the same level of trade, normally the ex-factory level, and of sales made at as nearly as possible the same time.

As part of the Agreement's requirements regarding transparency and participation, the investigating authorities are required to inform parties of the information needed to ensure a fair comparison, for instance, information regarding adjustments, allowances, and currency conversion, and may not impose an "unreasonable burden of proof" on parties.

Allowance

To ensure that prices are comparable, the Agreement requires that adjustments be made to either the normal value, or the export price, or both, to account for differences in the product, or in the circumstances of sale, in the importing and exporting markets. These allowances must be made for differences in conditions and terms of sale, taxation, quantities, physical characteristics, and other differences demonstrated to affect price comparability.

Adjustments in case of constructed export price

The Agreement also provides specific rules on the adjustment to be made if the comparison of normal value is to a constructed export price. In those circumstances, allowance must be made for costs, including duties and taxes, incurred between the importation of the product and the resale to the first independent purchaser, as well as for profits accruing. If price comparability has been affected, the Agreement requires either that the normal value be established at a level of trade equivalent to that of the constructed export price, which is likely to require an adjustment, or allowance must be made for differences in conditions and terms of sale, taxation, quantities, physical characteristics, and other matters demonstrated to affect price comparability.

Conversion of currency

Where the comparison of normal value and export price requires conversion of currency, the Agreement provides specific rules governing that conversion (Article 2.4.1). Thus, the exchange rate used should be that in effect on the date of sale (date of contract, invoice, purchase order or order confirmation, whichever establishes material terms of sale). If a forward currency sale is directly linked to export sale, the exchange rate of forward currency sale must be used. Moreover, the Agreement requires that exchange rate fluctuations be ignored, and that exporters be allowed at least 60 days to adjust export prices for sustained exchange rate movements.

CALCULATION OF DUMPING MARGINS AND DUTY ASSESSMENT

Calculation of dumping margins

The Agreement contains rules governing the calculation of dumping margins. In the usual case, the Agreement requires either the comparison of the weighted average normal value to the weighted average of all comparable export prices, or a transaction-to-transaction comparison of normal value and export price (Article 2.4.2). A different basis of comparison can be used if there is "targeted dumping": that is, if a pattern exists of export prices differing significantly among different purchasers, regions or time periods. In this situation, if the investigating

authorities provide an explanation as to why such differences cannot be taken into account in weighted average-to-weighted average or transaction-to-transaction comparisons, the weighted average normal value can be compared to the export prices on individual transactions.

Refund or reimbursement

The Agreement requires Members to collect duties on a non-discriminatory basis on imports from all sources found to be dumped and causing injury, except with respect to sources from which a price undertaking has been accepted. Moreover, the amount of the duty collected may not exceed the dumping margin, although it may be a lesser amount. The Agreement specifies two mechanisms to ensure that excessive duties are not collected. The choice of mechanism depends on the nature of the duty collection process. If a Member allows importation and collects an estimated anti-dumping duty, and only later calculates the specific amount of anti-dumping duty to be paid, the Agreement requires that the final determination of the amount must take place as soon as possible, upon request for a final assessment. In both cases, the Agreement provides that the final decision of the authorities must normally be made within 12 months of a request for refund or final assessment, and that any refund should be made within 90 days.

Individual exporter dumping margins

The Agreement requires that, when anti-dumping duties are imposed, a dumping margin be calculated for each exporter. However, it is recognized that this may not be possible in all cases, and thus the Agreement allows investigating authorities to limit the number of exporters, importers, or products individually considered, and impose an anti-dumping duty on uninvestigated sources on the basis of the weighted average dumping margin actually established for the exporters or producers actually examined. The investigating authorities are precluded from including in the calculation of that weighted average dumping margin any dumping margins that are de minimis, zero, or based on the facts available rather than a full investigation, and must calculate an individual margin for any exporter or producer who provides the necessary information during the course of the investigation.

New shippers

The Agreement makes provision for the assessment of anti-dumping duties on exports from producers or exporters who were not sources of imports considered during the period of investigation. In this circumstance, the investigating authorities are required to conduct an expedited review to determine a specific margin of dumping attributable to the exports of such a “new shipper”. While that review is in progress, the authorities may request guarantees or withhold appraisement on imports, but may not actually collect anti-dumping duties on those imports.

DETERMINATION OF INJURY AND CASUAL LINK

Like product (Article 2.6)

An important decision must be made early in each investigation to determine the domestic “like product”. Like product is defined in the Agreement as “a product which is identical, i.e. alike in all respects to the product under consideration or, in the absence of such a product, another product which, although not alike in all respects, has characteristics closely resembling those of the product under consideration”. The determination involves first examining the imported product or products that are alleged to be dumped, and then establishing what domestically produced product or products are the appropriate “like product”. The decision regarding the like product is important because it is the basis of determining which companies constitute the domestic industry, and that determination in turn governs the scope of the investigation and determination of injury and causal link.

Domestic industry (Article 4)

The Agreement defines the term “domestic industry” to mean “the domestic producers as a whole of the like products or those of them whose collective output of the products constitutes a major proportion of the total domestic production of those products”.

Related domestic producers

The Agreement recognizes that in certain circumstances, it may not be appropriate to include all producers of the like product in the domestic industry. Thus, Members are permitted to exclude from the domestic industry producers related to the exporters or importers under investigation, and producers who are themselves importers of the allegedly dumped product. The Agreement provides that a producer can be deemed “related” to an exporter or importer of the allegedly dumped product if there is a relationship of control between them, and if there is reason to believe that the relationship causes the domestic producer to behave differently from non-related producers.

Regional domestic industry

The Agreement contains special rules that allow in exceptional circumstances, consideration of injury to producers comprising a “regional industry”. A regional industry may be found to exist in a separate competitive market if producers within that market sell all or almost all of their production of the like product in that market, and demand for the like product in that market is not to any substantial degree supplied by producers of the like product located outside that market. If this is the case, investigating authorities may find that injury exists, even if a major proportion of the entire domestic industry, including producers outside the region, is not materially injured. However, a finding of injury to the regional industry is only allowed if (1) there is a concentration of dumped imports into the market served by the regional industry, and (2) dumped imports are causing injury to the producers of all or almost all of the production within that market.

Imposition of duties in regional industry cases

If an affirmative determination is based on injury to a regional industry, the Agreement requires investigating authorities to limit the duties to products consigned for final consumption in the region in question, if constitutionally possible. If the Constitutional law of a Member precludes the collection of duties on imports to the region, the investigating authorities may levy duties on all imports of the product, without limitation, if anti-dumping duties cannot be limited to the imports from specific producers supplying the region. However, before imposing those duties, the investigating authorities must offer exporters an opportunity to cease dumping in the region or enter a price undertaking.

INJURY

Types of injury

The Agreement provides that, in order to impose anti-dumping measures, the investigating authorities of the importing Member must make a determination of injury. The Agreement defines the term “injury” to mean either (i) material injury to a domestic industry, (ii) threat of material injury to a domestic industry, or (iii) material retardation of the establishment of a domestic industry, but is silent on the evaluation of material retardation of the establishment of a domestic industry.

Basic requirements for determination of material injury

The Agreement does not define the notion of “material”. However, it does require that a determination of injury must be based on positive evidence and involve an objective examination of (i) the volume of dumped imports and the effect of the dumped imports on prices in the domestic market for like products, and (ii) the consequent

impact of the dumped imports on domestic producers of the like product. Article 3 contains some specific additional factors to be considered in the evaluation of these two basic elements, but does not provide detailed guidance on how these factors are to be evaluated or weighed, or on how the determination of causal link is to be made.

Basic requirements for determination of threat of material injury

The Agreement sets forth factors to be considered in the evaluation of threat of material injury. These include the rate of increase of dumped imports, the capacity of the exporter(s), the likely effects of prices of dumped imports, and inventories. There is no further elaboration on these factors, or on how they are to be evaluated. The Agreement does, however, specify that a determination of threat of material injury shall be based on facts, and not merely on allegation, conjecture, or remote possibility, and moreover, that the change in circumstances which would create a situation where dumped imports caused material injury must be clearly foreseen and imminent.

ELEMENTS OF ANALYSIS

Consideration of volume effects of dumped imports

The Agreement requires investigating authorities to consider whether there has been a significant increase in the dumped imports, either in absolute terms or relative to production or consumption in the domestic industry. Consideration of price effects of dumped imports.

Consideration of price effects of dumped imports

In addition, the Agreement requires investigating authorities to consider whether there has been significant price undercutting by the dumped imports as compared with the price of a like product of the importing Member. Investigating authorities are also required to consider whether the effect of dumped imports is “otherwise” to depress prices to a significant degree, or to prevent price increases, which otherwise would have occurred, to a significant degree.

Evaluation of volume and price effects of dumped imports

The Agreement provides that no one or several of these factors can necessarily give decisive guidance. It does not specify how the investigating authorities are to evaluate the volume and price effects of dumped imports: merely that consideration of these effects is required. Thus, investigating authorities have to develop analytical methods for undertaking the consideration of these factors. Moreover, since no single factor or combination of factors will necessarily result in either an affirmative or negative determination, in each case investigating authorities have to evaluate which factors are relevant, and which are important, in light of the circumstances of the particular case at issue.

Examination of impact of dumped imports on the domestic industry

The Agreement provides that, in examining the impact of dumped imports on the domestic industry, the authorities are to evaluate all relevant economic factors bearing upon the state of the domestic industry. The Agreement lists a number of factors which must be considered, including actual or potential declines in sales, profits, output, market share, productivity, return on investments, utilization of capacity, actual or potential effects on cash flow, inventories, employment, wages, growth, ability to raise capital or investments, and the magnitude of the margin of dumping. However, the list is not exhaustive, and other factors may be deemed relevant. In addition, the Agreement again specifies that no single factor or combination of factors will necessarily lead to either an affirmative or negative determination.

Demonstration of causal link

The Agreement requires a demonstration that there is a causal relationship between the dumped imports and the injury to the domestic industry. This demonstration must be based on an examination of all relevant evidence. The Agreement does not specify particular factors or give guidance in how relevant evidence is to be evaluated. Article 3.5 does require, however, that known factors other than dumped imports which may be causing injury must be examined, gives examples of factors (such as changes in the pattern of demand, and developments in technology) which may be relevant, and specifies that injury caused by such "other factors" must not be attributed to dumped imports. Thus, the investigating authorities must develop analytical methods for determining what evidence is or may be relevant in a particular case, and for evaluating that evidence, taking account of other factors which may be causing injury.

Cumulative analysis

Cumulative analysis refers to the consideration of dumped imports from more than one country on a combined basis in assessing whether dumped imports cause injury to the domestic industry. Obviously, since such analysis will increase the volume of imports whose impact is being considered, there is a greater possibility of an affirmative determination in a case involving cumulative analysis. The practice of cumulative analysis was the subject of much controversy under the Tokyo Round Code, and in the negotiations for the Agreement. Article 3.3 of the Agreement establishes the conditions in which a cumulative evaluation of the effects of dumped imports from more than one country may be undertaken. The authorities must determine that the margin of dumping from each country is not de minimis, that the volume of imports from each country is not negligible, and that a cumulative assessment is appropriate in light of the conditions of competition among the imports and between the imports and the domestic like product. De minimis dumping margins and negligible import volumes are defined in the Agreement.

INVESTIGATION

Initiation

Agreement Article 5 of the Agreement establishes the requirements for the initiation of investigations. The Agreement specifies that investigations should generally be initiated on the basis of written request submitted "by or on behalf of" a domestic industry. This "standing" requirement includes numerical limits for determining whether there is sufficient support by domestic producers to conclude that the request is made by or on behalf of the domestic industry, and thereby warrants initiation. The Agreement establishes requirements for evidence of dumping, injury, and causality, as well as other information regarding the product, industry, importers, exporters, and other matters, in written applications for anti-dumping relief, and specifies that, in special circumstances when authorities initiate without a written application from a domestic industry, they shall proceed only if they have sufficient evidence of dumping, injury, and causality. In order to ensure that investigations without merit are not continued, potentially disrupting legitimate trade, Article 5.8 provides for immediate termination of investigations in the event the volume of imports is negligible or the margin of dumping is de minimis, and establishes numeric thresholds for these determinations. In order to minimize the trade-disruptive effect of investigations, Article 5.10 specifies that investigations should be completed within one year, and in no case more than 18 months, after initiation.

Conduct

Article 6 of the Agreement sets forth detailed rules on the process of investigation, including the collection of evidence and the use of sampling techniques. It requires authorities to guarantee the confidentiality of sensitive information and verify the information on which determinations are based. In addition, to ensure the transparency of proceedings, authorities are required to disclose the information on which determinations are to be based to interested parties and provide them with adequate opportunity to comment. The Agreement establishes the

rights of parties to participate in the investigation, including the right to meet with parties with adverse interests, for instance in a public hearing. Further guidance on the conduct of investigations is contained in two Annexes to the Agreement, which set forth rules for the on-the-spot investigations to verify information obtained from foreign parties, as well as rules for the use of best information available in the event a party refuses access to, or does not provide, requested information, or significantly impedes the investigation.

PROVISIONAL MEASURES AND PRICE UNDERTAKINGS

Imposition of provisional measures

Article 7 of the Agreement provides rules relating to the imposition of provisional measures. These include the requirement that authorities make a preliminary affirmative determination of dumping, injury, and causality before applying provisional measures, and the requirement that no provisional measures may be applied sooner than 60 days after initiation of an investigation. Provisional measures may take the form of a provisional duty or, preferably, a security by cash deposit or bond equal to the amount of the preliminarily determined margin of dumping. The Agreement also contains time limits for the imposition of provisional measures— generally four months, with a possible extension to six months at the request of exporters. If a Member, in its administration of anti-dumping duties, imposes duties lower than the margin of dumping when these are sufficient to remove injury, the period of provisional measures is generally six months, with a possible extension to nine months at the request of exporters.

Price undertakings

Article 8 of the Agreement contains rules on the offering and acceptance of price undertakings, in lieu of the imposition of anti-dumping duties. It establishes the principle that undertakings between any exporter and the importing Member, to revise prices, or cease exports at dumped prices, may be entered into to settle an investigation, but only after a preliminary affirmative determination of dumping, injury and causality has been made. It also establishes that undertakings are voluntary on the part of both exporters and investigating authorities. In addition, an exporter may request that the investigation be continued after an undertaking has been accepted, and if a final determination of no dumping, no injury, or no causality results, the undertaking shall automatically lapse.

COLLECTION OF DUTIES

Imposition and collection of duties

Article 9 of the Agreement establishes the general principle that imposition of anti-dumping duties is optional, even if all the requirements for imposition have been met. It also states the desirability of application of a “lesser duty” rule. Under a lesser duty rule, authorities impose duties at a level lower than the margin of dumping if this level is adequate to remove injury. In addition, the Agreement contains rules intended to ensure that duties in excess of the dumping margin are not collected, and rules for applying duties to new shippers.

Retroactive application of duties

The Agreement sets forth the general principle that both provisional and final anti-dumping duties may be applied only as of the date on which the determinations of dumping, injury and causality have been made. However, recognizing that injury may have occurred during the period of investigation, or that exporters may have taken actions to avoid the imposition of an anti-dumping duty, Article 10 contains rules for the retroactive imposition of dumping duties in specified circumstances. If the imposition of anti-dumping duties is based on a finding of material injury, as opposed to threat of material injury or material retardation of the establishment of a domestic industry, anti-dumping duties may be collected as of the date provisional measures were imposed. If provisional duties were collected in an amount greater than the amount of the final duty, or if the imposition of duties is

based on a finding of threat of material injury or material retardation, a refund of provisional duties is required. Article 10.6 provides for retroactive application of final duties to a date not more than 90 days prior to the application of provisional measures in certain exceptional circumstances involving a history of dumping, massive dumped imports, and potential undermining of the remedial effects of the final duty.

REVIEW AND PUBLIC NOTICE

Duration, termination, and review of anti-dumping measures

Article 11 of the Agreement establishes rules for the duration of anti-dumping duties, and requirements for periodic review of the continuing need, if any, for the imposition of anti-dumping duties or price undertakings. These requirements respond to the concern raised by the practice of some countries of leaving anti-dumping duties in place indefinitely. The “sunset” requirement establishes that dumping duties shall normally terminate no later than five years after first being applied, unless a review investigation prior to that date establishes that expiry of the duty would be likely to lead to continuation or recurrence of dumping and injury. This five year “sunset” provision also applies to price undertakings. The Agreement requires authorities to review the need for the continued imposition of a duty upon request of an interested party.

Public notice

Article 12 sets forth detailed requirements for public notice by investigating authorities of the initiation of investigations, preliminary and final determinations, and undertakings. The public notice must disclose non-confidential information concerning the parties, the product, the margins of dumping, the facts revealed during the investigation, and the reasons for the determinations made by the authorities, including the reasons for accepting and rejecting relevant arguments or claims made by exporters or importers. These public notice requirements are intended to increase the transparency of determinations, with the hope that this will increase the extent to which determinations are based on fact and solid reasoning.

REGULATORY FRAMEWORK FOR ANTI DUMPING IN INDIA

India is firmly committed to the principle of free and fair trade among nations, which is the very foundation of the multilateral trade order established by WTO. While a giant step has been taken by India towards establishment of free trade regime with the phasing out of Quantitative Restrictions on imports, there is also a need to ensure fair trade. Depending upon the need, anti-dumping, anti-subsidy countervailing and safeguard measures have been invoked in the past.

All these measures are in the nature of trade remedies, which the domestic industry could take advantage of subject to the fulfilment of essential conditions and criteria as mandated under law. The government has already put in place the requisite legal and institutional mechanism for administering these measures. However, various concepts and legal and operational aspects involved in these schemes need to be understood in the proper sense and in the right perspective.

Under the existing WTO arrangement, and in terms of various provisions under the Customs Tariff Act of 1975 (as amended in 1995) and Rules framed there under, anti-dumping and allied measures constitute the legal framework, within which the domestic industry can seek necessary relief and protection against dumping of goods and articles by exporting companies and firms of any country from any part of the world. These measures have assumed a great deal of relevance in India in recent times in view of the scenario arising out of unfair trade practices adopted by some of the trading partners, especially in the post-QR phase.

The Anti-Dumping and allied measures are complex legal disciplines which are often not within the easy comprehension of the trade and industry who are the users of these measures. To obviate this difficulty faced by large sections of the domestic industry, there is a need to explain the basic concepts, legal provisions

and procedural aspects in clear and easy language for their benefit. This will facilitate the domestic industry to avail of these remedial measures in the wake of alleged dumping and of injury caused by unfair trade practices.

However, it is always necessary to bear in mind that the anti-dumping action can never be an action based on presumption and vague complaints and only on very rare occasions suo-moto proceedings can be initiated. The requisite parameters of law have to be duly complied with and need to be fully supported and substantiated with facts and figures before any action could be initiated.

Sections 9, 9 A, 9 B and 9 C of the Customs Tariff Act, 1975 as amended in 1995 and the Customs Tariff (Identification, Assessment and Collection of Anti-dumping Duty on Dumped Articles and for Determination of Injury) Rules, 1995 framed there under form the legal basis for anti-dumping investigations and for the levy of anti-dumping duties. These laws are based on the Agreement on Anti-Dumping which is in pursuant of Article VI of GATT 1994.

Legal Framework

- *Based on Article VI of GATT 1994*
- *Customs Tariff Act, 1975 - Sec 9A, 9B (as amended in 1995)*
- *Anti-Dumping Rules [Customs Tariff (Identification, Assessment and Collection of Anti Dumping Duty on Dumped Articles and for Determination of Injury) Rules, 1995]*
- *Investigations and Recommendations by Designated Authority, Ministry of Commerce*
- *Imposition and Collection by Ministry of Finance*

INSTITUTIONAL ARRANGEMENT IN INDIA FOR ANTI DUMPING

Anti dumping duties in India are administered by the Directorate General of Anti dumping and Allied Duties (DGAD) functioning in the Dept. of Commerce in the Ministry of Commerce and Industry and the same is headed by the “Designated Authority”. The Designated Authority’s function, however, is only to conduct the anti dumping/anti subsidy & countervailing duty investigation and make recommendation to the Government for imposition of anti dumping or anti subsidy measures. Such duty is finally imposed/levied by a Notification of the Ministry of Finance. Thus, while the Department of Commerce recommends the Anti-dumping duty, it is the Ministry of Finance, which levies such duty.

Safeguard measures, on the other hand, are administered by another Authority namely, Director General (Safeguard), which functions under the Dept. of Revenue, Ministry of Finance. The Standing Board of Safeguards (chaired by the Commerce Secretary) considers the recommendations of the DG (Safeguards) and then recommends the impositions of the Safeguard Duty as it deems fit, to the Ministry of Finance which levies the duty.

ANTI DUMPING DUTIES – PROCEDURES IN INDIA

Dumping is said to have taken place when an exporter sells a product to India at a price less than the price prevailing in its domestic market. However, the phenomenon of dumping is per se not condemnable as it is recognized that producers sell their goods at different prices to different market. It is also not unusual for prices to vary from time to time in the light of supply and demand conditions. It is also recognized that price discrimination in the form of dumping is a common international commercial practice. It is also not uncommon that the export prices are lower than the domestic prices.Therefore, from the point of view of anti- dumping practices, there is nothing inherently illegal or immoral about the practice of dumping. However, where dumping causes or threatens to cause material injury to the domestic industry of India, the Designated Authority initiates necessary action for investigations and subsequent imposition of anti-dumping duties.

Determination of Dumping

Dumping occurs when the export price of goods imported into India is less than the Normal Value of 'like articles' sold in the domestic market of the exporter. Imports at cheap or low prices do not per se indicate dumping. The price at which like articles are old in the domestic market of the exporter is referred to as the "Normal Value" of those articles.

Normal Value

The normal value is the comparable price at which the goods under complaint are sold, in the ordinary course of trade, in the domestic market of the exporting country or territory. If the normal value cannot be determined by means of domestic sales, the Act provides for the following two alternative methods:

- Comparable representative export price to an appropriate third country.
- Cost of production in the country of origin with reasonable addition for administrative, selling and general costs and profits.

Export Price

The export price of goods imported into India is the price paid or payable for the goods by the first independent buyer.

Constructed Export Price

If there is no export price or the export price is not reliable because of association or a compensatory arrangement between the exporter and the importer or a third party, the export price may be constructed on the basis of the price at which the imported articles are first resold to an independent buyer. If the articles are not resold as above or not resold in the same condition as imported, their export price may be determined on a reasonable basis.

Margin of Dumping

Margin of dumping refers to the difference between the Normal Value of the like article and the Export Price of the product under consideration. Margin of dumping is normally established on the basis of:-

- a comparison of weighted average Normal Value with a weighted average of prices of comparable export transactions; or
- comparison of normal values and export prices on a transaction to transaction basis.

A Normal Value established on a weighted average basis may be compared to prices of individual export transactions if the Designated Authority finds a pattern of export prices that differ significantly among different purchasers, regions, time period, etc. It is significant to note that the alternative method of comparing the normal values and export prices is a major change introduced after the Uruguay Round.

The margin of dumping is generally expressed as a percentage of the export price.

Illustration: Normal value US$ 110 per kg. Export price US$ 100 per kg. There is dumping in this case as export price is lower than normal value and dumping margin in this case is US$ 10 per kg., i.e. 10% of the export price.

Factors Affecting Comparison of Normal Value and Export Price

The export price and the normal value of the goods must be compared at the same level of trade, normally at the ex-factory level, for sales made as near as possible in time. Due allowance is made for differences that affect price comparability of a domestic sale and an export sale. These factors, inter alia, include:

- Physical characteristics

- Levels of trade
- Quantities
- Taxation
- Conditions and terms of sale

It must be noted that the above factors are only indicative and any factor which can be demonstrated to affect the price comparability, is considered by the Authority.

Like Articles

Anti-dumping action can be taken only when there is an Indian industry which produces “like articles” when compared to the allegedly dumped imported goods. The article produced in India must either be identical to the dumped goods in all respects or in the absence of such an article, another article that has characteristics closely resembling those goods.

Injury to the Domestic Industry

The Indian industry must be able to show that dumped imports are causing or are threatening to cause material injury to the Indian ‘domestic industry’. Material retardation to the establishment of an industry is also regarded as injury.

The material injury or threat thereof cannot be based on mere allegation, statement or conjecture.

Sufficient evidence must be provided to support the contention of material injury. Injury analysis can broadly be divided in two major areas:

(i) The Volume Effect: The Authority examines the volume of the dumped imports, including the extent to which there has been or is likely to be a significant increase in the volume of dumped imports, either in absolute terms or in relation to production or consumption in India, and its affect on the domestic industry.

(ii) The Price Effect:

The effect of the dumped imports on prices in the Indian market for like articles, including the existence of price undercutting, or the extent to which the dumped imports are causing price depression or preventing price increases for the goods which otherwise would have occurred. The consequent economic and financial impact of the dumped imports on the concerned Indian industry can be demonstrated, inter alia, by:

- decline in output
- loss of sales
- loss of market share
- reduced profits
- decline in productivity
- decline in capacity utilization
- reduced return on investments
- price effects
- adverse effects on cash flow, inventories, employment, wages, growth, investments, ability to raise capital, etc.

Injury analysis is a detailed and intricate examination of all the relevant factors. It is not necessary that all the factors considered relevant should individually show injury to the domestic industry.

Causal Link

A 'causal link' must exist between the material injury being suffered by the Indian industry and the dumped imports. In addition, other injury causes have to be investigated so that they are not attributed to dumping. Some of these are volume and prices of imports not sold at dumped prices, contraction in demand or changes in the pattern of consumption, export performance, productivity of the domestic industry etc.

Who can File an Application

A dumping investigation can normally be initiated only upon receipt of a written application by or on behalf of the "Domestic Industry".

In order to constitute a valid application, the following two conditions have to be satisfied :

- The domestic producers expressly supporting the application must account for not less than 25% of the total production of the like article by the domestic industry in India; and
- The domestic producers expressly supporting the application must account for more than 50% of the total production of the like article by those expressly supporting and those opposing the application.

Domestic Industry

Domestic industry means the Indian producers of like articles as a whole or those producers whose collective output constitutes a major proportion of total Indian production. Producers who are related to the exporters or importers or are themselves importers of the allegedly dumped goods shall be deemed not to form part of the domestic industry.

Relief to the Domestic Industry

Relief can be provided to the domestic industry in the form of anti- dumping duties or price undertakings.

1. Anti-Dumping Duties: Duties are imposed on a source specific basis and can be expressed either on ad valoren or specific basis. Non-cooperative exporters are required to pay the residuary duty, which is generally the highest of the co-operative exporters.

Lesser Duty Rule

Under the GATT provisions, the national authorities cannot impose duties higher than the margin of dumping. It is, however, suggested that it would be desirable if the appropriate Government authorities impose a lesser duty which is adequate to remove the injury to the domestic industry. Under the Indian laws, the Government is obliged to restrict the anti-dumping duty to the lower of the two i.e. dumping margin and the injury margin.

Injury Margin

Besides the calculation of the margin of dumping, the Designated Authority also calculates the injury margin which is the difference between the fair selling price due to the domestic industry and the landed cost of the product under consideration. Landed cost for this purpose is taken as the assessable value under the Customs Act and the basic customs duties.

De Minimis Margins

Any exporter whose margin of dumping is less than 2% of the export price shall be excluded from the purview of anti-dumping duties even if the existence of dumping, injury as well as the causal link are established.

Further, investigations against any country are required to be terminated if the volume of the dumped imports from that particular source are found to be below 3% of the total imports, provided the cumulative imports from all those countries who individually account for less than 3%, are not more than 7%.

2. Price Undertakings: The Designated Authority may suspend or terminate investigation if the exporter concerned furnished an undertaking to revise his price to remove the dumping or the injurious effect of dumping as the case may be. No undertaking can however be accepted before preliminary determination is made. No anti-dumping duties are recommended on such exporters from whom price undertaking has been accepted. No price undertaking may, however, be accepted in case it is found that acceptance of such undertaking is impracticable or is unacceptable for any reason.

The Application Procedure

Applications can be made by or on behalf of the concerned domestic industry to the Designated Authority in the Ministry of Commerce for an investigation of any alleged dumping. The designated Authority may initiate an investigation when there is sufficient evidence that dumped imports are causing or are threatening to cause material injury to the Indian industry producing like articles or are materially retarding the establishment of an industry. Copies of the prescribed application proforma is available from the Ministry of Commerce.

Information Required

Applications should be submitted to the Designated Authority in the Ministry of Commerce in the prescribed form. Guidelines on how to complete a questionnaire are a part of the prescribed application proforma. The proforma also advises the applicant of the type of evidence required in appropriate areas.

Period of Investigation

Neither the GATT Agreement on anti-dumping nor the Indian laws provide for any specific guidelines regarding the period of investigation. However, there are indications that the period should not be, in any case, less than six months. It is, however, important that the period taken into consideration for detailed investigation should be representative and as recent as possible.

Confidential Information

Any information provided to the Designated Authority on a confidential basis by any party shall not be disclosed to any other party without the specific authorization of the party providing the information, if the Designated Authority is satisfied about its confidentiality. Interested parties supplying information on a confidential basis are required to furnish non-confidential summaries thereof or a statement of reasons as to why such summarization is not possible.

If the Designated Authority is not satisfied that the confidentiality is warranted or the provider of information is not willing to disclose it in a generalized form, then such information may be disregarded.

Investigation Process

An application received by the Designated Authority is dealt with as follows :

1. Preliminary Screening: The application is scrutinized to ensure that it is adequately documented and provides sufficient evidence for initiation. If the evidence is not adequate, then a deficiency letter is issued normally within 20 days of the receipt of the application.

2. Initiation: When the Designated Authority is satisfied that there is sufficient evidence in the application with regard to dumping, material injury and causal link, a Public Notice is issued initiating an investigation to determine the existence and effect of the alleged dumping.

The Designated Authority notifies the diplomatic representative of the Government of the exporting country before proceeding to initiate the investigation.

The initiation notice will be issued normally within 45 days of the date of receipt of a properly documented application.

3. Access to Information: The Authority provides access to the non-confidential evidence presented to it by various interested parties in the form of a public file, which is available for inspection after receipt of the responses.

4. Preliminary Findings: The Designated Authority will proceed expeditiously with the conduct of the investigation and shall, in appropriate cases, make a preliminary finding containing the detailed information on the main reasons behind the determination. The preliminary finding will normally be made within 150 days of the date of initiation.

5. Provisional Duty: A provisional duty not exceeding the margin of dumping may be imposed by the Central Government on the basis of the preliminary finding recorded by the Designated Authority. The provisional duty can be imposed only after the expiry of 60 days from the date of initiation of investigation. The provisional duty will remain in force only for a period not exceeding 6 months, extendable to 9 months under certain circumstances.

6. Oral Evidence: Interested parties who participate in the investigations can request the Designated Authority for an opportunity to present the relevant information orally. However, such oral information shall be taken into consideration only when it is subsequently reproduced in writing. The Authority may grant oral hearing anytime during the course of the investigations.

7. Final Determination: The final determination is normally made within 150 days of the date of preliminary determination.

8. Disclosure of Information: The Designated Authority will inform all interested parties of the essential facts which form the basis for its decision before the final finding is made.

9. Time-limit for Investigation Process: The normal time allowed by the statute for conclusion of investigation and submission of final findings is one year from the date of initiation of the investigation. The above period may be extended by the Central Government by 6 months.

10. Termination: The Designated Authority may suspend or terminate the investigation in the following cases :

(i) if there is a request in writing from the domestic industry at whose instance the investigation was initiated.

(ii) when there is no sufficient evidence of dumping or injury.

(iii) if the margin of dumping is less than 2% of the export price.

(iv) the volume of dumped imports from a country is less than 3% of the total imports of the like article into India or the volume of dumped imports collectively from all such countries is less than 7% of the total imports.

(v) injury is negligible.

Other Provisions

Retrospective Measures

The Act provides for levy of anti-dumping duty retrospectively, where -

(i) there is a history of dumping which caused the injury or that the importer was, or, should have been aware that the exporter practices dumping and that such dumping would cause injury, and

(ii) the injury is caused by massive dumping, in a relatively short time, so as to seriously undermine the remedial effect of anti-dumping duty.

(iii) Such retrospective application will not go beyond 90 days of the date of imposition of provisional duty. Further, no retrospective application prior to the date of initiation of investigation is possible.

Review

An anti-dumping duty imposed under the Act shall have the effect for 5 years from the date of imposition, unless revoked earlier.

The Designated Authority shall also review the need for the continued imposition of the anti-dumping duty, from time to time. Such a review can be done suo motu or on the basis of request received from an interested party in view of the changed circumstances. A review shall also follow the same procedures prescribed for an investigation to the extent they are applicable.

The Designated Authority is also required to carry out a review for determining margins of dumping for any new exporter or producer from a country that is subject to anti-dumping, provided that these exporters or producers are new and are not related to any of the exporters or producers who are subject to anti-dumping duty on the product.

Appeal

An appeal against the order of the Designated Authority may be filed with the Customs, Excise and Gold (Control) Appellate Tribunal within 90 days of the date of the order.

Refund of Duty

If the anti-dumping duty imposed on the basis of final findings is higher than the provisional duty already imposed and collected, the difference shall not be collected.

If the final anti-dumping duty is less than the provisional duty already imposed and collected, the difference shall be refunded.

If the provisional duty is withdrawn based on a negative final finding, then the provisional duty already collected shall be refunded.

Miscellaneous

Products Imported by Units in EPZS/100% EOUS, Advance Licence Holders and by other Exporters

Anti-dumping duty is not payable on products imported by units in EPZs and 100% EOUs, as well as imports on products imported by advance licence holders in terms of Customs notification No. 41/97-Cus dated 30.4.1997.

The final anti-dumping duty paid on imported goods used in the manufacture of export goods are liable to be refunded as duty drawback in accordance with the drawback rules.

Applicability of Anti-dumping Duties vis á vis Other Measures

GATT agreement as well as the Indian laws provide that the injured domestic industry is permitted to file for relief under the anti-dumping as well as countervailing duties. However, no articles shall be subjected to

both countervailing and anti-dumping duties to compensate for the same situation of dumping or export subsidization.

ANTI DUMPING CASES INITIATED BY INDIA

Anti-dumping investigations initiated by all countries, were at a high in 2001 declined almost steadily till 2007. They picked up once again in 2008 but started decline to reach a low in 2011. However, in 2012 they have again increased with 114 investigations (up to June) compared to 68 in 2011 (up to June). In 2011 India topped the list of countries initiating such investigations, but in 2012 (up to June) Brazil is at the top followed by Argentina and Canada.

India, the US, and EU with seven investigations each are at fourth spot. During 2012-13 (1.4.2012 to 31.12.2012), 10 fresh cases have been initiated by the Directorate General of Anti-dumping and Allied Duties (DGAD). The countries involved in these investigations are China PR, the European Union, Korea RP, Malaysia, Mexico, Taiwan, Thailand, Turkey, Saudi Arabia, and the USA.

Investigation initiated by top ten users of Anti-Dumping Measures 1995-2012

Country	1995	2001	2002	2003	2005	2007	2008	2009	2010	2011	2011	2012	1995-2012*
India	6	79	81	46	28	47	55	31	41	19	10	7	663
United States	14	77	35	37	12	28	16	20	3	15	9	7	465
European Union	33	28	20	7	24	9	19	15	15	17	8	7	444
Argentina	27	28	14	1	12	8	19	28	14	7	4	10	301
Brazil	5	17	8	4	6	13	23	9	37	16	11	26	258
Australia	5	24	16	8	7	2	6	9	7	18	2	6	241
South Africa	16	6	4	8	23	5	3	3	0	4	1	0	216
China	0	14	30	22	24	4	14	17	8	5	0	4	195
Canada	11	25	5	15	1	1	3	6	2	2	0	10	165
Turkey	0	15	18	11	12	6	23	6	2	2	1	6	154
All Countries	157	372	315	234	201	165	213	209	172	155	68	114	4125

Source: WTO **Upto June 2012*

OTHER REMEDIAL MEASURES AGAINST UNFAIR TRADE PRACTICES IN ADDITION TO ANTI DUMPING IN INDIA

Apart from dumping, some of the countries also resort to subsidisation of their exports to other countries. Export subsidies, under the WTO agreement, are treated as unfair trade practice and such subsidies are actionable by way of levy of anti-subsidy countervailing duty.

Safeguards

There is one more trade remedial measure called “safeguards” which are applied as an emergency measure in response to surge in imports of a particular item. Safeguards are applied when :

- there is a surge in imports of a particular product irrespective of a particular country/ies and,
- it causes serious injury to the domestic industry.

Safeguard measures are applied to all imports of the product in question irrespective of the countries in which it originates or from which it is exported. This aspect distinguishes Safeguards from anti dumping and anti subsidy measures which are always country specific and exporter specific. Safeguards are applied in the form of either

safeguard duty or in the form of safeguard QRs (import licenses). These measures are administered in India by an Authority called Director General (Safeguards) who functions in the jurisdiction of the Department of Revenue, Ministry of Finance.

Anti subsidy countervailing measure

It is in the form of countervailing duty which is to be imposed only after the determination that:

- the subsidy is a specific subsidy
- the subsidy relates to export performance;
- the subsidy relates to the use of domestic goods over imported goods in the export article; or
- the subsidy has been conferred on a limited number of persons engaged in manufacturing, producing or exporting the article.

For this purpose a subsidy is said to exist;

(a) if there is a financial contribution by the Government or any public body within the territory of the exporting country, i.e. where-

- there is a direct transfer of funds (including grants, loans and equity) by the Government;
- government revenue i.e. otherwise due is foregone and not collected (including fiscal incentives, I.T. exemption
- a government provides goods or services other than general infrastructure;

(b) a government grants or maintains any form of income or price support which operates directly or indirectly to increase export of any article from its territory.

Following is not a subsidy

The subsidy which is for research activities conducted by the persons engaged in manufacture or export or the subsidy which is for assistance to disadvantaged regions with the territory of the exporting country is not actionable. Thus, no countervailing duty is to be levied on such subsidies.

In anti subsidy countervailing investigation, the Government of the exporting country/ies is also a party to the investigation in addition to the exporters from these countries.

The countervailing duty imposed on the subsidised exports from a country shall not exceed the amount of such subsidy/ies.

RECENT ANTI DUMPING CASES IN INDIA

1. Indonesian CTV picture tubes attract dumping duty

The Finance Ministry of India has slapped anti-dumping duty of US$21.76 per unit on imports of 14-inch cathode ray colour television (CRT) picture tubes from *PT LP Displays Indonesia*. The duty is being levied for five years from March 2009 onwards. Notably, colour picture tubes account for 40-45 percent of television production cost. Given that the monthly capacity of the domestic tube industry is short of a million pieces or significantly less than the domestic market size for colour TV, the mentioned high cost share has significant implications for the welfare effects of antidumping duty. The revenue department has also advocated levy of anti-dumping duty on colour television picture tubes sized 15, 20, 21 and 29 inches.

2. Definitive dumping duty on phosphoric acid from Korea

Following the petition filed by Gujarat Alkalies & Chemicals Ltd., and Solaris Chemtech, the Finance Ministry of India has levied anti-dumping duty of US$221.64/tonne on phosphoric acid from South Korea. The duty shall be applicable for five years from June 22, 2010.

3. The Phenol from European Union case - Transit or transshipment cannot change the country of origin or export of goods

In this case [2007 (209) E.LT. 303], the Hon'ble CESTAT held that the records clearly bring out that the goods in the present case are of Russian origin and exported from Russia. There was only transshipment from Finland. Transit or transshipment cannot change the country of origin or export of goods. Notification No.79/2002 imposed anti-dumping duty on European Union origin goods. In the present case since the goods were of Russian origin, anti-dumping duty was not attracted.

4. The NBR Case - Commercial substitutability and manufacturing process considered relevant

In the case of imports of Acrylonitrile Butadiene Rubber (NBR) from Japan (Notification No.25/ADD/94, dated the 19th October, 1995) the Designated Authority found that all Nitrile-rubbers are copolymers of Acrylonitrile and Butadiene and served the same general purpose of providing resistance to petroleum chemicals, though the same have different specific end applications. Variations in Acrylonitrile content merely enhance one of the general properties for which NBR is used. The manufacturing process, equipment and other facilities needed for producing different grades of NBR are common and do not involve any special equipment to produce different grades of NBR. The various users could switch their requirements between domestic and overseas product, which clearly established that the two were substitutable. The Ministry of Chemicals & Fertilizers, Department of Chemicals and Petrochemicals also gave the opinion that the two products/grades imported are 'like products' as manufactured domestically. The Designated Authority therefore, confirmed that NBR produced by the petitioner and that imported from Japan are 'like products' within the meaning of the Rules.

5. The Hot Rolled Coils Case – India: Normal value can be determined on the basis of price of similar article produced by others

In the Hot Rolled Coils case – India [2000 (116) E.L.T. 356 (Tribunal)], with regard to the normal value, the Hon'ble Tribunal observed that Clause (c) of Section 9A defines normal value. Sub-clause (i) of Clause (c) states that normal value means the comparable price in the ordinary curse of trade for the like article meant for consumption in the exporting country or territory as determined in accordance with the Rules. The comparable price in the ordinary course of trade mentioned in this sub-clause can only be the comparable price for the like article manufactured by the same exporter against whom investigation is undertaken by the Designated Authority. Price of the like article of any other manufacturer cannot be the basis for finding out the normal value for assessing the dumping margin or normal value. When such comparable price for the like article of the same manufacturer is not available, then sub-clause (ii) of Clause (c) comes into operation. This sub-clause contains two alternatives. The first alternative is comparable representative price of the like article when exported from the exporting country or territory to an appropriate country. When particular manufacturer/exporter who is stated to be dumping his produce in India has no sales of like article in the domestic market, then the representative price of that article when he exports to an appropriate country, can be the basis for finding the normal value. Normal value of the article can also be assessed as per the second alternative provided therein, namely, the cost of production of the article in the country of origin along with reasonable addition for administrative selling and general cost and for profits.

6. The Borax Decahydrate from Turkey Case – India

Determination of Export price: In the Borax Decahydrate imported from Turkey case—India, the Hon'ble Tribunal in its order 2007 (215) E.L.T. 33 (Tri.) held that the Designated Authority had rightly determined the export price. The Hon'ble Tribunal observed as under:

> "It was argued by the learned Counsel for the appellant that the determination of export price was not appropriate because various costs such as expenses incurred by Boro Chemi India, bank charges incurred by ETI Turkey and reasonable profit of Boro Chemi, Singapore had not been taken into account. It, however, appears from the record, that Boro Chemi India was not involved in the sales or after sales service of the product in India. The contention of the domestic industry that deductions should have been made of the expenses incurred by Boro Chemi India, bank charges incurred by the Turkish producer and reasonable profit of Singaporean exporter, while determining the export price, is misconceived. It transpires from the record that, the entire actual profit margin of Boro Chemi International, Singapore, the exporter, which was worked out at 18.6%, had been deducted in arriving at the ex-factory price. Moreover, the Turkish producer ETI had not incurred any bank charges on realization of the export proceeds, as was verified by the designated authority. No deductions were, therefore, required to be made in connection with the bank charges which were not incurred. It also transpires from the record that Boro Chemi India was manufacturing boric acid powder in its own unit in India. On examination of the record and the documents of Boro Chemi India, the designated authority concluded that it was not concerned with the subject goods and that there was no question of deducting any expenses of Boro Chemi India from the export price of Boro Chemi International, Singapore. It was found that the advertisement expenses were in fact paid by Boro Chemi Internationa, Singapore and not by Boro Chemi India, as per the invoices and payment details which were placed before the designated authority. Besides that, Boro Chemi India were not concerned with the goods except for a couple of solitary transactions discussed in paragraph 16A of the final findings, which have not been disputed before us."

7. The Bus and Truck Radial Tyres Case – India

In the bus and truck radial tyres from China and Thailand case 2011 (270) E.L.T. 696 (Tri.Del.), the Hon'ble Tribunal observed that the overall picture that emerged from examination of various injury parameters did not support the conclusion of injury drawn by the D.A.A. number of parameters such as capacity, production, capacity utilization, sales, selling prices and profitability of return on investment, wages, employment, productivity etc. recorded an improvement during the periods chosen for injury analysis. It was also submitted on behalf of the appellants that the domestic industry was suffering losses even before the period chosen for analysis and that the losses in fact came down to the lowest level during the POI. The Hon'ble tribunal observed that this case was in fact quite different from the kind of case dealt by the Hon'ble Supreme Court in the case of Rishiroop Polymers cited by the learned Advocate for the Domestic Industry, where there was a drastic decline in all the parameters during the POI. The Hon'ble Supreme Court in the case of Rishiroop Polymers Pvt. Ltd., v. Designate Authority—2006 (196) E.L.T. 129(S.C.) had observed as follows :

> "Having gone through the confidential records produced before us and the data for the years 1995-96 and 1996-97, we are satisfied that the domestic industry suffered drastic decline in all the relevant parameters during the period of investigation compared to those of the immediately preceding financial years 1995-96. We find no justification to take a view other than what ahs been taken by the Designated Authority and the Tribunal. Accordingly, the findings recorded by the Designated Authority as well as by the Tribunal on this point are confirmed".

In view of the above, the Hon'ble Tribunal set aside the Final Findings dated 1-1-2010 issued by the Designated Authority, Ministry of Commerce and the Customs Notification No.12/2010 issued by the Government of India, Ministry of Finance, Department of Revenue, New Delhi imposing anti-dumping duty on the subject goods based on such finding of the Designated Authority.

CASE STUDY - THE INDIAN SHRIMP INDUSTRY ORGANIZES TO FIGHT THE THREAT OF ANTI-DUMPING ACTION

This case study is taken from WTO website and it deals with the way in which the Indian shrimp industry responded when faced with an anti-dumping action in the United States. It also indicates the potential impact of the anti-dumping action on the fragmented, small-producers-dominated industry.

I. The case history

On 31 December 2003, the Ad Hoc Shrimp Trade Action Committee (ASTAC), an association of shrimp farmers in eight southern states of the United States, filed an anti-dumping petition against six countries — Brazil, China, Ecuador, India, Thailand and Vietnam. The petition alleged that these countries had dumped their shrimps in the US market. Though the actual petition was made by the Ad Hoc Shrimp Trade Action Committee, whose members are located in Alabama, Florida, Georgia, Louisiana, Mississippi, North Carolina, South Carolina and Texas, the Southern Shrimp Alliance (SSA) had been organizing the process of seeking redress.

The petition meeting statutory requirements, on 21 January 2004 the US Department of Commerce (DOC) announced the initiation of anti-dumping investigations against the six countries. Products covered include warm water shrimp, whether frozen or canned, wild caught (ocean harvested) or farm-raised (produced by aqua-culture), head-on or head-off, shell-on or peeled, tail-on or tail-off, deveined or not deveined, cooked or raw, or otherwise processed in frozen or canned form.

The Department notified the International Trade Commission (ITC) of its decision on initiation. On 17 February 2004 the International Trade Commission announced its decision that there was a reasonable indication that the US shrimp industry is materially injured or threatened with material injury by imports, allegedly at less than fair value, from the six identified countries. As a result, the Department of Commerce continued with its investigations and gave its preliminary determination on 28 July 2004. The ratio of preliminary duty varies between 3.56% and 27.49% for three mandatory respondents selected by the DOC. The weighted arranged rate for India is 14.2%, and the average rate for China is 49.09%, for Brazil 36.91%, for Vietnam 16.01%, for Ecuador 7.3% and for Thailand 6.39%.

II. The national and international context

The trouble had started much earlier than December 2003. On 26 February 2002, Reggie Dupre, a Louisiana state senator, alleged that tainted farm-raised Asian shrimp was being diverted from Europe and dumped on the US market. Dupre was calling for a congressional investigation into food safety and unfair pricing, as local fishermen voiced concern that imports had depressed the prices they got for the locally harvested shrimp. By September 2002, shrimp industry representatives from eight southern states had got together to fight the case against imported shrimp from certain countries. 'We stand a better chance of success when all shrimp-producing states come on board', as George Barisich, president of the United Commercial Fisherman's Association, observed.

On 22 October 2002, representatives of the shrimp industry from the eight southern states voted to form the Southern Shrimp Alliance to fight unfair competition from imported farm-raised shrimp from certain countries. There was, however, a basic problem. It was estimated that it might cost more than US$3 million in terms of legal expenses to go for an anti-dumping petition.

There were also problems associated with divergent trade interests. Shrimp importers and distributors were afraid that a long-drawn-out battle would affect the supply of imported shrimp and adversely affect their business. Wally Stevens, president of the American Seafood Distributors Association, described how the salmon industry in Maine had filed an anti-dumping petition against Norway in 1990, hoping to stabilize prices. Twelve years after winning and spending up to $10 million, salmon was selling at half the price prevailing at the time of the beginning of the dispute. 'This is definitely not the right way to go. It consumes an immense

amount of money and is not a long-term solution in terms of maintaining viability.' In a statement in January 2003, Stevens said that his organization, in support of 'free and fair trade', would oppose any anti-dumping action by the SSA.

In the meantime, countries threatened with the prospective action started reacting. Vietnam, one of the countries identified almost at the beginning of the SSA exercises and also highly dependent on the US market for shrimp exports, was the first to protest. Foreign Ministry spokeperson Phan Thuy Thanh said in a statement on 12 September 2002 that 'I can say with certainty that Vietnam has never dumped its shrimp, and its shrimp have been sold at market prices.' Thailand was another country to lodge a protest. Kenneth Pierce, of Willkie Farr & Gallagher, representing the Thai Frozen Foods Association, condemned the move to consider anti-dumping action against Thai shrimp exports. 'Thailand's shrimps have never been dumped in the United States, nor have they caused material damage to US shrimp', he said in a statement on 25 November 2002. As evidence mounted of the SSA's determination to go ahead with the petition on anti-dumping, other threatened countries also started taking preventive actions. Rokhmin Dahiri, the Indonesian Maritime and Fisheries Minister, denied allegations that the Indonesian government subsidized its shrimp farmers. He said in a statement on 25 August 2003 that the price of shrimp on the domestic market was much lower than the export price. The dumping charge was baseless and, therefore, the United States should exclude Indonesia from the proposed anti-dumping investigations. The government of Bangladesh took similar action, and Vietnam also started working out alliances. Nguyen Thi Hong Minh, Vietnamese Deputy Fisheries Minister, said in a statement on 4 August 2003 that the Vietnamese shrimp businesses and their counterparts in south-east Asia, India and China as well as US shrimp importers were considering measures including lobbying to prevent a lawsuit.

The Indian government and the Indian shrimp industry were aware of the threat. Arun Jaitley, the then Minister for Commerce, made a statement in June 2003 after his official visit to the United States: 'We are anticipating an action against our shrimp exports because our share in the US market is on the rise.' During the whole of 2003, the SSA went through the process of raising the required resources and trimming the number of countries against which dumping action was to be brought, as the cost of the legal battle increased with the number of countries. After a compromise with the Mexican shrimp industry, the number of countries was ultimately brought down to six.

The main contentions of the petitioners were as follows.

- The six named countries accounted for 74% of shrimp imports in the US market.
- Imports from the six countries increased from 466 million lb. in 2000 to 650 million lb in 2002.
- Import prices of the targeted countries had dropped by 28% in the previous three years. The average unit value of the targeted countries in 2000 was $3.54; this had fallen to $2.55 in 2002, on a headless, shell-on equivalent basis.
- The average dockside price for one count size of gulf shrimp dropped from $6.08 to $3.30 per pound from 2000 to 2002.
- The United States was the most open market in the world. High tariff rates in other large importing countries provided a powerful incentive for exporters to increase shrimp shipments to the United States. Likewise, the US market also served as the market of last resort when shrimp shipments were denied entry to other markets such as the European Union due to the discovery of unacceptable levels of contaminants.

III. The Indian shrimp industry and its response

The first concrete signal that India might be included in the US industry's anti-dumping petition was received by the Indian government in June 2003. That anti-dumping investigations against Indian shrimp imports

might be initiated was hinted at during bilateral talks when the then Commerce and Industry Minister Arun Jaitley had met his counterpart in Washington at that time. The reason given was that India's shrimp exports to the United States had been rising rapidly during the previous three years, from $255.93 million during 2000-1 to $299.05 million during 2002-3.

India's marine products industry has been one of the major export success stories. From an export base of just Rs. 450 million in 1971-2, it increased to Rs. 68,810 million in 2002-3. Shrimp is the mainstay of India's marine product exports.

Japan has traditionally been the biggest export market for India's marine products, followed by the United States, China and several EU countries. There was an over-dependence on the Japanese market, as shrimp is the major export item which Japan imports in huge volume. However, in the recent past, there has been a gradual decline in the intake from Japan with an increasing absorption in the United States, as well as some other countries. The United States, traditionally a buyer of small-sized shrimp from India, has now started buying many other varieties, including black tiger shrimp, resulting in its occupying the top slot in India's export markets of marine products, replacing Japan in 2002-3.

Success in India's shrimp export is directly attributable to the development of shrimp culture. Assisted by the Marine Products Export Development Authority (MPEDA), shrimp culture has developed as a major industry in several coastal states. It is mostly an enterprise of small and medium farmers, and has led to the utilization of otherwise unproductive areas in the coastal region, contributing to improvements in the socio-economic conditions of the rural poor in the shrimp farming areas. It has created direct employment of about 300, 000 people and indirect employment to over 700, 000.

The Indian government has played an important role in the promotion of marine product exports, including the development of shrimp farming. The MPEDA is a government-sponsored body whose mandate covers the development of the industry as a whole, including export promotion. It is under the administrative control of the Department of Commerce and is headed by a senior officer of the Indian Administrative Service. Its governing council comprises senior officials of the central and state governments as well as representatives of the marine products industry.

The Seafoods Exporters Association of India (SEAI) is the nodal body of the exporters community and is represented on the MPEDA governing council. There is, therefore, close co-ordination between these two bodies which are primarily responsible for organizing the shrimp industry's as well as the government's response to the US anti-dumping investigations.

After the statement of the Commerce Minister on the possible threat to Indian shrimp exports to the United States, these two bodies went into action. To explore the possibilities of avoiding the anti-dumping action and, if necessary, to take legal action, a delegation comprising senior members of the SEAI went to Washington in September 2003, and after discussions in various quarters, decided to sign an agreement with the law firm, Garvey Schubert and Barer, to be the counsel in the United States for the anti-dumping investigations. After returning to India, the SEAI informed its members through a circular letter that 'Ms Lisbeth Levinson, a partner in the firm, will personally and exclusively handle our case.'

Regarding the extremely damaging potential of the proposed anti-dumping action, the SEAI pointed out to its members that in July 2003 the United States had imposed anti-dumping duty ranging from 44% to 63% on catfish fillet imports from Vietnam which would remain in force for five years. There will be annual reviews to decide whether the duties need any adjustments upwards or downwards. The Association warned its members that any such move against India's shrimp exports would ring the death knell of the industry.

The Association also realized the importance of other related regulatory provisions for Indian shrimp exports to the United States. The SEAI informed its members that within twenty days of filing the case, the United States could start imposing anti-dumping duties which would be returned only if the Indian exporters won the

case. Since this anti-dumping duty would have to be paid by the US importers, the SEAI cautioned that they might stay away from India, and therefore the business would start to become affected long before the case came to its final conclusion.

The game plan worked out by the MPEDA and the SEAI was comprehensive. It involved approaching the central government, developing contacts with counterpart bodies in other countries which might be named in the petition, and putting their house in order, to raise resources.

By October 2003, the plan had started taking shape. In a statement on 8 October 2003, K. Jose Cyriac, the chairman of the MPEDA, said, 'We are discussing the issues with other countries which are likely to be labelled with dumping charges.'

The SEAI president, Abraham Tharakan, after describing the petition as extremely unfair, said that in addition to calling for government support it would seek to co-operate with major exporting associations in Vietnam, Thailand and China and to forge an alliance among the Asian exporters. Some twenty-five Indian companies export to the United States, and the industry anticipated that the case might be filed against six or seven big players. However, the SEAI decided to fight the case from the platform of the organization as a mark of solidarity.

'We will back each indicted company', said Ranjit Bhattacharye, secretary-general of the SEAI, whose management committee decided that it would defend the industry's position, meet the cost of the legal process and not leave the cost to be borne by those Indian firms that might be selected for investigations.

The SEAI has estimated a total budgetary requirement of Rs. 70 million to fight the case. Of this, SEAI would mobilize Rs. 40 million internally and the remaining Rs 30 million would be collected from its members, depending on the volume and value of their individual exports to the US market.

When the initiation decision came on 21 January 2004, both the organizations were unhappy, but they were expecting it and were therefore ready to act. According to the SEAI, 'with over 75% of the US producers having signed the petition, proceeding with the hearing was a fait accompli'.

Both Jose Cyriac and Abraham Tharakan left for the United States to take further action to protect the interests of the Indian shrimp exporters.

The SEAI had worked out plans to contest the dumping allegations on various grounds. It put forward two major differences between the Indian and the US sea-caught shrimp and offered reasons why Indian shrimp is cheaper.

First, there are specific variations between the shrimp caught off the south-west coast of the United States and in Indian waters, so that prices are bound to be different. 'The threat for the domestic shrimp farmer in the United States comes from China, Thailand, Indonesia and Ecuador. India's shrimp exports are predominantly of black tiger and scampi varieties which are not cultivated in the United States', according to the president of SEAI.

Second, while fishing in the United States is a capital-intensive activity calling for major investment, in India shrimp capture is carried out with a very low level of capital and requiring hardly any investment. This makes the cost of production considerably lower in India compared with that for shrimp sea-caught off the US coast.

Jose Cyriac observed, after the decision to initiate investigations, that the cost of cultured and captured shrimp in India was far lower than that of shrimp caught and bought in the US market, enabling Indian exporters to compete with US shrimp in price. Further, the petition filed before the US Department of Commerce had mixed up count and weight (shrimp is sold by size and the number of shrimp constituting 1 kg), providing another avenue to contest the case.

When the ITC decision on the preliminary affirmative decision came on 17 February 2004, the Indian shrimp

industry termed it 'discriminatory and unjust'. Tharakan of the SEAI said, 'We are deeply disappointed and upset by the verdict.' Asserting that the Indian shrimp industry has not been resorting to dumping, he was confident of ultimate victory: 'We have a strong case against US shrimpers. We are certain that we will win the case despite the setback.' Tharakan said that there was no possibility of the United States succeeding in imposing an anti-dumping duty on Indian shrimp as it was not sold below the cost price. On the contrary, it was sold to US importers at a price higher than that for Japan and for other countries.

On receipt of the preliminary decision, Indian exporters who were mobilizing funds said that they would fight the case till the end. Jose Cyriac commented: 'The government is unhappy with the US verdict. But it is only a preliminary finding. We will help the Indian exporters fight the case in the United States.'

The government itself came out with a statement on 18 February 2004, when S. N. Menon, special secretary in the Department of Commerce, said, 'We will fight it out. We are all geared up to fight the case and the industry has already hired lawyers for this.' Menon observed that India had a strong case as India was exporting mainly 'tiger shrimps which are not found there and that too, in unprocessed form'. Noting that 80% of shrimp consumption in the United States is met through imports, Menon said that unprocessed Indian shrimps generated about 1 million jobs in the US food processing industry, therefore, any action against Indian shrimp would adversely affect the US food processing sector. The SEAI and its members were getting ready for the next set of actions. After the preliminary positive determination by the ITC, the next step was for the Department of Commerce (ITA) to prove whether there had been dumping and at what level. As part of that exercise, a few leading firms would be selected from each country and detailed questionnaires would be sent to them.

According to Sandu Joseph, the secretary of the SEAI, a team of US DOC officials would visit Kerala, a major shrimp producing state, in June or early July. 'They will visit our shrimp farming factories and verify our accounting practices. Our factories and accounts are open. We want to prove that we are not producing and exporting cheap shrimp to the United States.'

Joseph also referred to the support the Association could mobilize in the United States. The SEAI had been receiving 'favourable support' from a group of US congressmen to fight the anti-dumping investigations. Joseph said that more than a dozen members of the Congress had written to US Commerce Secretary Donald Evans, asking him to use fair and reasonable procedures in the investigative process.

While the industry and the SEAI, as well as the Indian government, are fairly confident of the strength of their case, the biggest problem being faced by the shrimp exporters is the uncertainty caused by the anti-dumping investigations.

After the announcement of the preliminary ITC determination, Sandu Joseph commented that 'We have been badly affected. There is no shrimp export happening to the US now.' He said that Indian shrimp exporters had not received any export order from the United States since 17 February 2004.

By April 2004 there was widespread concern among the exporters, growers and other stakeholders. Shrimp exports to the United States had come almost to a standstill due to the uncertainty regarding the contingent applicability and incidence of the anti-dumping duty.

According to Joseph Zavier, general secretary of the Kerala Boat Owners Association, with almost insignificant exports to the United States since February the shrimp catch had been reduced by 40-45%. The price per kilogramme of white shrimps, Rs. 280 a few months previously, had crashed to Rs. 100 in April, while the price per kilogramme of another variety of prawn had fallen from Rs. 80 to Rs. 40.

In Tamil Nadu and Andhra Pradesh, two large southern states, shrimp farming is done in large barren areas converted into farms. Mohammad Nayeem, once a prosperous shrimp farmer in Andhra Pradesh, is now a broken man. He owns 100 acres of shrimp farm and used to sell the products at a price of Rs. 450-600 per kilogramme, but after the ITC decision the price had crashed to Rs. 220, while the cost of production was Rs. 250.

In Kerala, shrimp farming is mostly done in paddy fields, converted into shrimp farms, on the fringes of backwaters. According to Rajan P. Mambaly who is one of those who has given his land under lease for shrimp farming, the duty, if imposed, will hit him and the farmers hard, as the net price to the growers would come down to the extent of the anti-dumping duty.

The preliminary determination came on 28 July 2004. In a media briefing on 29 July 2004 the chairman of the MPEDA observed, 'We are not happy with the preliminary determination of the duty rates. The final determination would be on 16 December 2004 and we will fight the case further and try to bring it down to zero level.'

The investigation has now moved into the final determination stage. As part of the procedure, DOC officials visited India in August-September 2004 for onsite verification of the information and data submitted by the mandatory respondents during the preliminary phase of the investigations.

IV. WTO-related issues

India's shrimp export to the United States came under difficulties before, when the United States banned the import of captured shrimp from certain countries, including India, in 1976. It was on the ground that trawling for shrimp by mechanized means had been adversely affecting certain varieties of sea turtles. The dispute on the US ban on the import of shrimp caught without using turtle extruder devices during harvesting was taken to the WTO Dispute Settlement system by the affected countries, including India. The WTO ruled against the United States and asked it to make the regime WTO-compatible. However, since that had not yet happened, India's exports to the United States of aqua-culture shrimp and shrimp caught by non-mechanized means were being made on the basis of certification by the MPEDA, as required under the law.

The trade lobbyists in the United States, such as the Consuming Industries Trade Action Coalition (CITAC), the Seafood Distributors Association and others which were against the imposition of anti-dumping duties on imported shrimp, have raised the issue of the Continued Dumping or Subsidy Offset Act 2000, popularly known as the Byrd Amendment. They want the Act to be repealed or modified to make it WTO-compatible.

Under the Amendment, the US government distributes the anti-dumping and anti-subsidy duties to the US firms that brought forward the cases.

The Act was perceived to violate WTO rules by several countries. Eleven members of the WTO (Australia, Brazil, Canada, Chile, India, Indonesia, Japan, South Korea, Mexico, Thailand and the EU) requested the establishment of a Panel, while six others (Argentina, Costa Rica, Hong Kong, China, Israel and Norway) joined as third parties, supporting the complainants.

On 16 September 2002, the Panel Report recommended the repeal of the Byrd Amendment, as it was held to be a WTO-incompatible response to dumping and subsidization. Offset payments constitute a remedy, in addition to the imposition of an anti-dumping or anti-subsidy duty and this is not envisioned under the WTO rules. Following a US appeal in October 2002, the Appellate Body in its report in January 2003 confirmed the Panel's central finding that the Byrd Amendment is WTO-inconsistent.

The deadline for the US to bring the Byrd Amendment into WTO conformity expired on 27 December 2003. As a consequence, the EU has requested the WTO to authorize retaliatory measures in January 2004. The issue is currently before the WTO and the United States has, as yet, taken no action towards ensuring WTO compliance. However, at the meeting of the WTO Negotiating Group on Rules (26-28 April 2004), the United States said that it was 'beyond question that countries have the sovereign right to distribute government revenues as they deem appropriate', but added that the United States intended to implement the Byrd Amendment ruling.

Read the above case study carefully and identify the lessons learnt by the Indian Shrimp industry.

Hints:

- The crisis caused by the anti-dumping petition of the Ad Hoc Group has been so far handled competently. The two nodal agencies, one a government body (the MPEDA) and the other a private trade body (the SEAI) have co-ordinated their approaches.
- Several visits by the representatives of those two bodies to Washington at critical points also helped to bring an understanding of the nature of the problem and how to face it. This resulted in the selection and appointment of the legal counsel, as early as September 2003. The importance of co-ordinated action by the threatened partners, even those outside India, was appreciated and was worked on by the trade representatives with their counterparts in several Asian countries included in the petition.
- Another achievement has been the speedy resolution of the issue of financing. The fact that the Association decided to bear more than 50% of the total costs from its internal resources and the rest from the contribution of members according to the value of their respective exports was critical. Equally critical has been the government's steadfast support for the shrimp industry.
- But what remains unaddressed is the issue which is in fact generic and therefore affects all cases, including the shrimp case. Anti-dumping cases take a long time to be finally decided. During this period, trade is affected because importers are risk-avoiders and will, therefore, be likely to shift to new sources of supply until the uncertainty is resolved. Industry people pointed out that an anti-dumping case was initiated against Indian leather goods in South Africa two years ago. Although the case was ultimately settled in India's favour, the market was lost to India, because of the uncertainty caused by the transitional decisions.
- There is, therefore, a huge human element in such cases where the products originate in small and medium-sized enterprise sectors, and a large number of poor and marginal farmers, artisans or unskilled or semi-skilled labour are engaged in the production of such goods. As of now, there is no institutional mechanism, in the form of a safety net, to take care of this problem. The Indian shrimp industry is one where the problem is acute because of the way in which it is organized. As observed earlier, the industry is fragmented and dominated by small fishermen and farmers. Uncertainty for any reason create risks which they are not equipped to bear. This case has highlighted the need for the government to look at this issue. Since the Indian government has already indicated its decision to fight an adverse judgment, the need is more acute.

The shrimp industry in India had always focused on one or two major markets for growth. Previously it was Japan and during the last few years, it has been the United States. It has now learnt the importance of diversification.

LESSON ROUND UP

- Dumping is broadly defined as exporting at prices below those charged in the domestic market or at prices insufficient to cover the cost of the goods sold
- Dumping can be also characterized as international price discrimination, as predatory pricing or as intermittent dumping.
- Anti dumping is a measure to rectify the situation arising out of the dumping of goods and its trade distortive effect.The anti dumping duty is levied over and above the normal customs duty chargeable on the import of goods in consideration.
- Margin of dumping is the difference between the Normal value and the export price of the goods under complaint.
- Non-Injurious Price (NIP) is that level of price, which the industry is, expected to have charged under

normal circumstances in the Indian market during the Period defined.

– Price discrimination implies charging of significantly different product prices to two or more customers when there are no significant differences between the costs to the sellers for supplying to those customers.

– Predatory pricing is the second characterization of dumping that gives rise to an economic rationale for antidumping laws. It consists of systematically pricing below cost with a view to intimidating and eliminating rivals in an effort to bring about a market price higher than otherwise would prevail.

– Intermittent dumping occurs due to oversupply of perishable goods.

– The Agreement on Implementation of Article VI of GATT 1994 is commonly known as the Anti-Dumping Agreement (or the AD Agreement).

– Dumping is calculated on the basis of a "fair comparison" between normal value (the price of the imported product in the "ordinary course of trade" in the country of origin or export) and export price (the price of the product in the country of import).

– The basic requirement for determinations of injury, is that there be an objective examination, based on positive evidence of the volume and price effects of dumped imports and the consequent impact of dumped imports on the domestic industry.

– The AD Agreement requires investigating authorities to give public notice of and explain their determinations at various stages of the investigative process in substantial detail.

– The AD Agreement specifies that investigations should generally be initiated based on a written request submitted "by or on behalf of" a domestic industry.

– Disputes in the anti-dumping area are subject to binding dispute settlement before the Dispute Settlement Body of the WTO, in accordance with the provisions of the Dispute Settlement Understanding ("DSU") (Article 17).

– Indian laws were amended with effect from 1.1.1995 to bring them in line with the anti-dumping provisions in WTO Agreement. Anti-dumping duty investigations are carried out under Section 9A of the Customs Tariff Act, 1975 read with Section 9B and the rules made thereunder.

– Anti dumping duties in India are administered by the Directorate General of Anti dumping and Allied Duties (DGAD) functioning in the Dept. of Commerce in the Ministry of Commerce and Industry and the same is headed by the "Designated Authority".

– Anti-dumping action can be taken only when there is an Indian industry which produces "like articles" when compared to the allegedly dumped imported goods.

– The paramount objective of the multi-lateral trade regime of WTO is to establish free and fair international trade. With removal of QRs, India has moved towards the regime of free trade. At the same time, anti dumping measures can be applied, where warranted, in the interest of fair trade.

SELF TEST QUESTIONS

1. What do you mean by the term 'Dumping'? Explain the provisions of dumping under World Trade Prganization.
2. Write short notes on:
   (a) Price discrimination;
   (b) Predatory pricing;

(c) Margin of Dumping.

(d) Differnce between anti dumping duty and customs duty.

3. 'Injury Analysis can be broadly classified into two categories'. Elucidate.
4. Whether the Designated Authority can suspend or terminate the investigation? Discuss with the help of decided cases.
5. Explain the procedure for Anti-dumping investigations.
6. Discuss some of the important provisions of anti dumping agreement under WTO.
7. How is normal value of goods determined? Explain citing some of the recent cases in India.

Lesson 9
Subsidies and Countervailing Duties

LESSON OUTLINE

- Subsidy
- Difference between Dumping and Subsidy
- Countervailing Duty
- Anti Dumping Duty and Countervailing Duty
- WTO Provisions on Subsidies and Countervailing Duties
- Agreement on Subsidies And Countervailing Measures
- Legal Framework with respect to imposition of Anti-Subsidy in India
- Implementing Authorities in India
- Doha Development Round
- Recent Case Studies
- LESSON ROUND UP
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

Subsidies may play an important role in developing countries and in the transformation of centrally-planned economies to market economies. A subsidy is a grant or other financial assistance given by one party for the support or development of another. Subsidy has been used by economists with different meanings and connotations in different contexts. According to one OECD definition, "A subsidy is a measure that keeps prices for consumers below market levels, or keeps prices for producers above market levels or that reduces costs for both producers and consumers by giving direct or indirect support." This form of support can be legal, illegal, ethical or unethical. Subsidies are used for a variety of purposes, including employment, production and exports.

In this chapter subsidies in international prespective, countervailing duties and provisions of WTO regarding subsidies have been discussed in detail.

The only reason for a government service is precisely to provide financial support for an operation that is otherwise unsustainable, or else there would be no point in the government's involvement at all.

Lew Rockwell

SUBSIDY

In common parlance, the term subsidy means money granted by the State or a Public Body to keep the prices of commodities under control. Subsidy may take the form of direct or indirect government grants on production or exportation of goods including any special subsidy on transportation of any product. The subsidy is usually given to remove some type of burden and is often considered to be in the interest of the public.

There are many forms of subsidies given out by the government, including welfare payments, housing loans, student loans and farm subsidies. For example, if a domestic industry, like farming, is struggling to survive in a highly competitive international industry with low prices, a government may give cash subsidies to farms so that they can sell at the low market price but still achieve financial gain. If a subsidy is given out, the government is said to subsidize that group/industry.

Subsidies are often regarded as a form of protectionism or trade barrier by making domestic goods and services artificially competitive against imports. Subsidies may distort markets, and can impose large economic costs. Financial assistance in the form of a subsidy may come from one's government, but the term subsidy may also refer to assistance granted by others, such as individuals or non-governmental institutions.

DIFFERENCE BETWEEN DUMPING AND SUBSIDY

Dumping is an action adopted by individuals or enterprises and whereas, subsidy is action adopted by the Government or supported by the action of the Government.

WTO is an organization formed by negotiations between member nations to promote free international trade. In this regard, member nations have signed an undertaking and where necessary have also made necessary legislative provisions to seek consistency with common international agreements and negotiations. Accordingly, subsidy being an action of the Government, it becomes easier for the member nations to seek enforcement of the provisions that deviate from the undertakings and negotiations entered into between them. However, as dumping is an action of an undertaking in the country of another, member nations cannot normally seek enforcement but are permitted to take counter measures, which can prevent the intended damage.

COUNTERVAILING DUTY

A duty placed on imported goods that are being subsidized by the importing government is called countervailing duty. This helps to even the playing field between the domestic producers and the foreign producers receiving subsidies. Subsidized goods allow a producer to sell at a lower price than it could without the subsidy compensation. If this producer sells into the international market, they can often undercut the pricing of producers in other countries who don't receive subsidies from their government. If the subsidized foreign producer goes unchecked, the domestic producers could be run out of business, causing lost jobs and other economic losses. So a duty is levied on such imports, which is countervailing duty.

ANTI DUMPING DUTY AND COUNTERVAILING DUTY

Dumping and subsidies together with anti-dumping (AD) measures and countervailing duties (CVD) share a number of similarities. Many countries handle the two under a single law, apply a similar process to deal with them and give a single authority responsibility for investigations. Occasionally, the two WTO committees responsible for these issues meet jointly.

The reaction to dumping and subsidies is often a special offsetting import tax (countervailing duty in the case of a subsidy). This is charged on products from specific countries and therefore it breaks the GATT principles of binding a tariff and treating trading partners equally (MFN). The agreements provide an escape clause, but they

both also say that before imposing a duty, the importing country must conduct a detailed investigation that shows properly that domestic industry is hurt.

But there are also fundamental differences, and these are reflected in the agreements.

Dumping is an action by a company. With subsidies, it is the government or a government agency that acts, either by paying out subsidies directly or by requiring companies to subsidize certain customers.

But the WTO is an organization of countries and their governments. The WTO does not deal with companies and cannot regulate companies' actions such as dumping. Therefore the Anti-Dumping Agreement only concerns the actions governments may take against dumping. With subsidies, governments act on both sides: they subsidize and they act against each others' subsidies. Therefore the subsidies agreement disciplines both the subsidies and the reactions.

WTO PROVISIONS ON SUBSIDIES AND COUNTERVAILING DUTIES

The WTO Agreement on Subsidies and Coutervailing Duties : It disciplines the use of subsidies, and it regulates the actions countries can take to counter the effects of subsidies. It says a country can use the WTO's dispute settlement procedure to seek the withdrawal of the subsidy or the removal of its adverse effects. Or the country can launch its own investigation and ultimately charge extra duty (known as "countervailing duty") on subsidized imports that are found to be hurting domestic producers.

The agreement contains a definition of subsidy. It also introduces the concept of a "specific" subsidy — i.e. a subsidy available only to an enterprise, industry, group of enterprises, or group of industries in the country (or state, etc) that gives the subsidy. The disciplines set out in the agreement only apply to specific subsidies. They can be domestic or export subsidies.

The agreement defines two categories of subsidies: prohibited and actionable. It originally contained a third category: non-actionable subsidies. This category existed for five years, ending on 31 December 1999, and was not extended. The agreement applies to agricultural goods as well as industrial products, except when the subsidies are exempt under the Agriculture Agreement's "peace clause", due to expire at the end of 2003.

Prohibited subsidies**:** Subsidies that require recipients to meet certain export targets, or to use domestic goods instead of imported goods. They are prohibited because they are specifically designed to distort international trade, and are therefore likely to hurt other countries' trade. They can be challenged in the WTO dispute settlement procedure where they are handled under an accelerated timetable. If the dispute settlement procedure confirms that the subsidy is prohibited, it must be withdrawn immediately. Otherwise, the complaining country can take counter measures. If domestic producers are hurt by imports of subsidized products, countervailing duty can be imposed.

Actionable subsidies**:** in this category the complaining country has to show that the subsidy has an adverse effect on its interests. Otherwise the subsidy is permitted. The agreement defines three types of damage they can cause. One country's subsidies can hurt a domestic industry in an importing country. They can hurt rival exporters from another country when the two compete in third markets. And domestic subsidies in one country can hurt exporters trying to compete in the subsidizing country's domestic market. If the Dispute Settlement Body rules that the subsidy does have an adverse effect, the subsidy must be withdrawn or its adverse effect must be removed. Again, if domestic producers are hurt by imports of subsidized products, countervailing duty can be imposed.

Some of the disciplines are similar to those of the Anti-Dumping Agreement. Countervailing duty (the parallel of anti-dumping duty) can only be charged after the importing country has conducted a detailed investigation similar to that required for anti-dumping action. There are detailed rules for deciding whether a product is being subsidized (which is not always an easy calculation), criteria for determining whether imports of subsidized products are hurting ("causing injury to") domestic industry, procedures for initiating and conducting investigations,

and rules on the implementation and duration (normally five years) of countervailing measures. The subsidized exporter can also agree to raise its export prices as an alternative to its exports being charged countervailing duty.

Subsidies may play an important role in developing countries and in the transformation of centrally-planned economies to market economies. Least-developed countries and developing countries with less than $1,000 per capita GNP are exempted from disciplines on prohibited export subsidies. Other developing countries were given until 2003 to get rid of their export subsidies. Least-developed countries must have eliminated import-substitution subsidies (i.e. subsidies designed to help domestic production and avoid importing) by 2003 — for other developing countries the deadline was 2000. Developing countries also receive preferential treatment if their exports are subject to countervailing duty investigations. For transition economies, prohibited subsidies had to be phased out by 2002. Ultimately all forms of export subsidies should be phased out for free international trade between countries.

AGREEMENT ON SUBSIDIES AND COUNTERVAILING MEASURES

The Agreement on Subsidies and Countervailing Measures ("SCM Agreement") addresses two separate but closely related topics: multilateral disciplines regulating the provision of subsidies, and the use of countervailing measures to offset injury caused by subsidized imports.

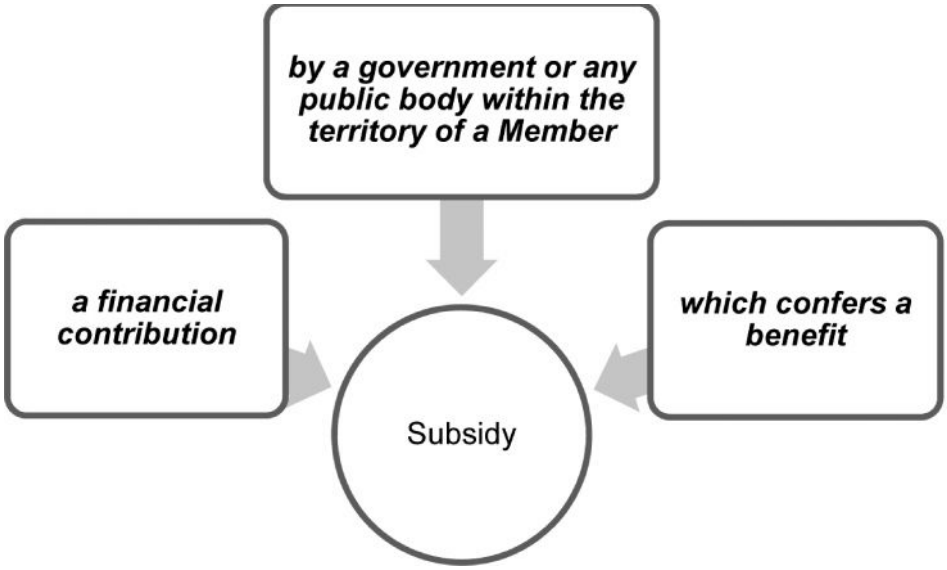
Multilateral disciplines are the rules regarding whether or not a subsidy may be provided by a Member. They are enforced through invocation of the WTO dispute settlement mechanism. Countervailing duties are a unilateral instrument, which may be applied by a Member after an investigation by that Member and a determination that the criteria set forth in the SCM Agreement are satisfied.

Structure of the Agreement

Part I	– Part I provides that the SCM Agreement applies only to subsidies that are specifically provided to an enterprise or industry or group of enterprises or industries, and defines both the term "subsidy" and the concept of "specificity."
Part II, II and IV	– Parts II, III and IV divide all specific subsidies into one of three categories – prohibited, actionable, and non-actionable, and establish certain rules and procedures with respect to each category.
Part V	– Part V establishes the substantive and procedural requirements that must be fulfilled before a Member may apply a countervailing measure against subsidized imports. Parts VI and VII establish the institutional structure and notification/ surveillance modalities for implementation of the SCM Agreement.
Part VIII	– It contains special and differential treatment rules for various categories of developing country Members.
Part IX	– It contains transition rules for developed country and former centrally planned economy Members.
Part X and XI	– Parts X and XI contain dispute settlement and final provisions.

Definition of subsidy

Article 1 of the Agreement on Subsidies and Countervailing Measures (Agreement on SCM) defines subsidy as involving a financial contribution by a government or any public body within the territory of a member or any form of income or price support which confers a benefit on the recipient. The definition of the term "subsidy" contains three basic elements. All three of these elements must be satisfied in order for a subsidy to exist.



(i) a financial contribution : The Agreement requires a financial contribution and contains a list of the types of measures that represent a financial contribution, e.g., grants, loans, equity infusions, loan guarantees, fiscal incentives, the provision of goods or services, the purchase of goods.

(ii) by a government or any public body within the territory of a Member: In order for a financial contribution to be a subsidy, it must be made by or at the direction of a government or any public body within the territory of a Member. Thus, the SCM Agreement applies not only to measures of national governments, but also to measures of sub-national governments and of such public bodies as state-owned companies.

(iii) which confers a benefit: A financial contribution by a government is not a subsidy unless it confers a "benefit." In many cases, as in the case of a cash grant, the existence of a benefit and its valuation will be clear. In some cases, however, the issue of benefit will be more complex. For example, when does a loan, an equity infusion or the purchase by a government of a good confer a benefit? Although the SCM Agreement does not provide complete guidance on these issues, the Appellate Body has ruled (Canada – Aircraft) that the existence of a benefit is to be determined by comparison with the market-place (i.e., on the basis of what the recipient could have received in the market). In the context of countervailing duties, Article 14 of the SCM Agreement provides some guidance with respect to determining whether certain types of measures confer a benefit.

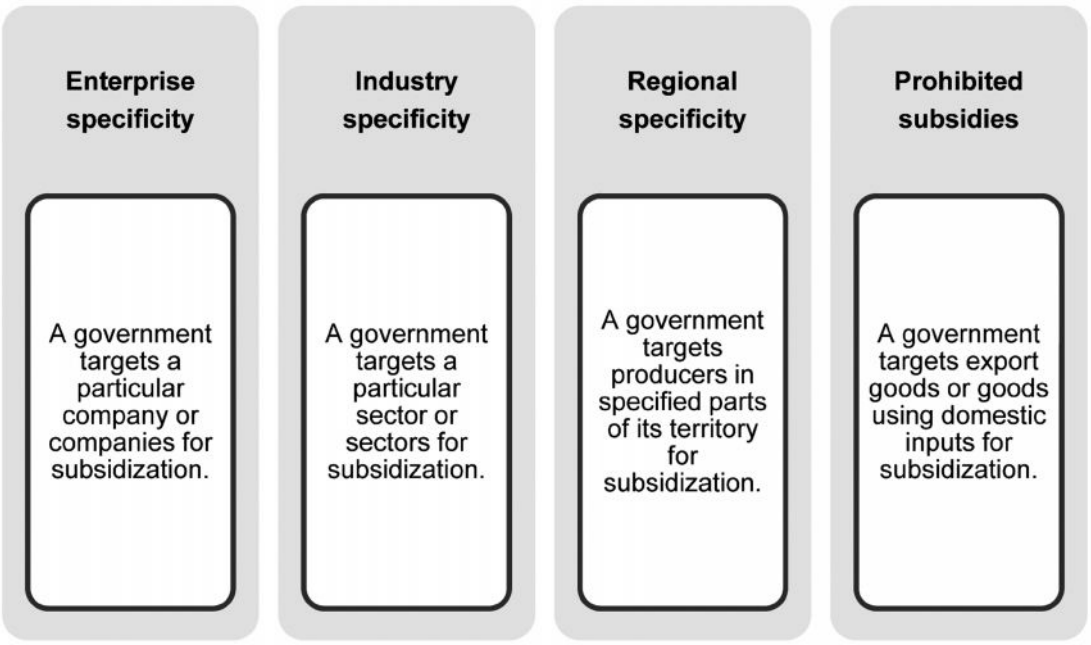
'Subsidy' has been defined to mean any financial contribution provided by aGovernment or a Public Body in the form of transfer of funds, tax incentives,provision of goods or service or any other form of income or price support by which a benefit is conferred.

Definition of Specificity

Article 2 of the Agreement on SCM provides a subsidy to be treated as specific if its availability is restricted only to the specified recipients i.e. to a specific enterprise or industry or a group of enterprises or industries (referred to as 'certain enterprises'). The following principles may determine whether a subsidy is specific:

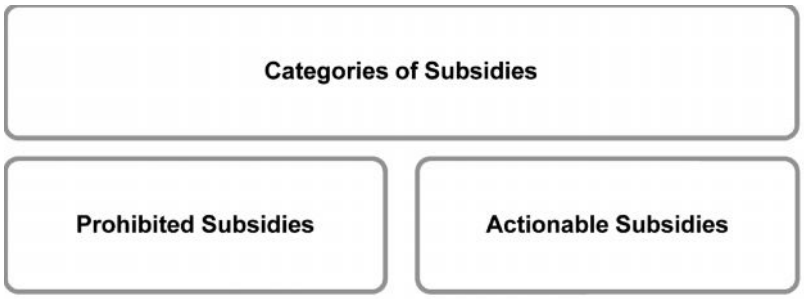
- where the granting authority, or the legislation pursuant to which the granting authority operates, explicitly limits access to a subsidy to certain enterprises, such subsidy shall be specific.
- where the eligibility for grant of subsidy is governed by objective criteria i.e. which are neutral and do not favour certain enterprises over others, which are economic in nature and horizontal in application, such as number of employees or size of enterprises etc and the eligibility is automatic; specificity shall not exist.
- if there are reasons to believe that a subsidy programme, though not specific in accordance with the above principles, in fact is for use by a limited number of certain enterprises or for predominant use of certain enterprises or if the discretion is so used that the benefits flow to certain enterprises, the subsidy shall be specific.

The basic principle is that a subsidy that distorts the allocation of resources within an economy should be subject to discipline. Where a subsidy is widely available within an economy, such a distortion in the allocation of resources is presumed not to occur. And only "specific" subsidies are subject to the SCM Agreement disciplines. There are four types of "specificity" within the meaning of the SCM Agreement:



Categories of subsidies

The SCM Agreement creates two basic categories of subsidies: those that are prohibited, those that are actionable (i.e., subject to challenge in the WTO or to countervailing measures). All specific subsidies fall into one of these categories.



1. Prohibited subsidies: Subsidies that require the recipients to meet certain export targets or to use domestic goods instead of imported goods would fall under the category of prohibited subsidies. They are prohibited because they are specifically designed to distort international trade and are therefore likely to hurt trade between countries.



2. Actionable subsidies: Subsidies which have an adverse effect on the interest of the complaining country, which may or may not be the importing country but whose interest are said to be affected adversely. An actionable subsidy may be of three types i.e. those which arise when any subsidy hurts the domestic industry of importing country, or is such which has the effect of reducing the share of the competing country in the competing export market, or is such which make the imported goods uncompetitive to domestic goods.

Most subsidies, such as production subsidies, fall in the "actionable" category. Actionable subsidies are not prohibited. However, they are subject to challenge, either through multilateral dispute settlement or through countervailing action, in the event that they cause adverse effects to the interests of another Member. There are three types of adverse effects.

- First, there is injury to a domestic industry caused by subsidized imports in the territory of the complaining Member. This is the sole basis for countervailing action.
- Second, there is serious prejudice. Serious prejudice usually arises as a result of adverse effects (e.g., export displacement) in the market of the subsidizing Member or in a third country market. Thus, unlike injury, it can serve as the basis for a complaint related to harm to a Member's export interests.
- ~~Finally, there is nullification or impairment of benefits accruing under the GATT 1994. Nullification or impairment arises most typically where the improved market access presumed to flow from a bound tariff reduction is undercut by subsidization.~~

Special Rules on Agricultural subsidies: Article 13 of the Agreement on Agriculture establishes, during the implementation period specified in that Agreement (until 1 January 2003), special rules regarding subsidies for agricultural products. Export subsidies which are in full conformity with the Agriculture Agreement are not prohibited by the SCM Agreement, although they remain countervailable. Domestic supports which are in full conformity with the Agriculture Agreement are not actionable multilaterally, although they also may be subject to countervailing duties. Finally, domestic supports within the "green box" of the Agriculture Agreement are not actionable multilaterally nor are they subject to countervailing measures. After the implementation period, the SCM Agreement shall apply to subsidies for agricultural products subject to the provisions of the Agreement on Agriculture, as set forth in its Article 21.

Point to Remember

When subsidy is considered to be unfair: Subsidy is a benefit provided to a particular class of persons when they meet a certain specified criteria. The subsidy would become unfair, when by virtue of the benefit so provided, it creates an unfair advantage to such class of persons, providing better than needed competitive advantage and diluting the level playing field in internationally competitive price sensitive market.

Countervailing Measures

Part V of the SCM Agreement sets forth certain substantive requirements that must be fulfilled in order to impose a countervailing measure, as well as in-depth procedural requirements regarding the conduct of a countervailing investigation and the imposition and maintenance in place of countervailing measures. A failure to respect either the substantive or procedural requirements of Part V can be taken to dispute settlement and may be the basis for invalidation of the measure.

1. Substantive rules: A Member may not impose a countervailing measure unless it determines that there are subsidized imports, injury to a domestic industry, and a causal link between the subsidized imports and the injury. As previously noted, the existence of a specific subsidy must be determined in accordance with the criteria in Part I of the Agreement. However, the criteria regarding injury and causation are found in Part V. One significant development of the new SCM Agreement in this area is the explicit authorization of cumulation of the effects of subsidized imports from more than one Member where specified criteria are fulfilled. In addition, Part V contains rules regarding the determination of the existence and amount of a benefit.

2. Procedural rules: Part V of the SCM Agreement contains detailed rules regarding the initiation and conduct of countervailing investigations, the imposition of preliminary and final measures, the use of undertakings, and the duration of measures. A key objective of these rules is to ensure that investigations are conducted in a transparent manner, that all interested parties have a full opportunity to defend their interests, and that investigating authorities adequately explain the bases for their determinations.

A few of the more important innovations in the WTO SCM Agreement are identified below:

- ***Standing:*** The Agreement defines in numeric terms the circumstances under which there is sufficient support from a domestic industry to justify initiation of an investigation.
- ***Preliminary investigation:*** The Agreement ensures the conduct of a preliminary investigation before a preliminary measure can be imposed.
- ***Undertakings:*** The Agreement places limitations on the use of undertakings to settle CVD investigations, in order to avoid Voluntary Restraint Agreements or similar measures masquerading as undertakings
- ***Sunset:*** The Agreement requires that a countervailing measure be terminated after five years unless it is determined that continuation of the measure is necessary to avoid the continuation or recurrence of subsidization and injury.

– ***Judicial review:*** The Agreement requires that Members create an independent tribunal to review the consistency of determinations of the investigating authority with domestic law.

Parameters Determining Countervailing Measures

Types of subsidies against which action is permitted: Action against subsidy is normally in the form of levy of countervailing duty by the importing country, which would be equivalent to the amount of subsidy provided by the exporting country. In this regard, subsidies that are specifically provided to an enterprise or industry or group of enterprises or industries are restricted and against which action is permissible. This is for the reason that subsidies of such nature can distorts the allocation of resources within an economy and accordingly is subjected to discipline. In case a subsidy is widely available within an economy, then such a distortion in the allocation of resources is presumed not to occur. Accordingly, only subsidies that are specific are subjected to the levy of countervailing duty.

Exempted specific subsidies: The following subsidies have been exempted even if they are considered to be specific:

– research activities conducted by or on behalf of persons engaged in the manufacture, production or export; or

– assistance to disadvantaged regions within the territory of the exporting country; or

– assistance to promote adaptation of existing facilities to new environmental requirements.

When can an action be taken against subsidy?

In case subsidy has been provided by a member nation of WTO, then the complaining member may request the member, providing subsidy to come for consultations so as to clarify on the facts and to arrive at a mutually agreed solution. In case where mutually agreed solution is not reached within 30 days of the request for consultations, any Member, party to such consultations may refer the matter to the Dispute Settlement Body ("DSB"), which on investigation if found that the measure in question is a prohibited subsidy, then it would recommend that the subsidizing Member should withdraw the subsidy without delay. In the event that the subsidizing member does not follow the recommendations of the DSB, within the time-period specified by the panel, then the DSB would grant the complaining Member specific authorization to take countervailing measures. In case subsidy is provided by a non-member nation of the WTO, then the nation is allowed to take appropriate countervailing measures without following the procedure of consultation or through the dispute settlement body.

When does a nation resort to countervailing measure?

Countervailing measures would mean levy of countervailing duty on import of specified subsidized articles. The countervailing measures would be resorted only when the subsidizing nation refuses to remove/ withdraw the specific subsidy. Further, countervailing measures are levied only when subsidies are of such nature that causes serious injury to the domestic industry.

Determination of injury

The determination of injury for purposes of levy of countervailing duty against subsidy would be based on positive evidence, which would normally involve an objective examination of

(a) the volume of the subsidized imports and the effect it has on the prices in the domestic market for like products and

(b) the consequent impact of these imports on domestic producers of such products.

Definition of injury

The term "injury" has been defined to mean either

(i) material injury to a domestic industry,

(ii) threat of material injury to a domestic industry, or

(iii) material retardation of the establishment of a domestic industry. Thus, there needs to be either an actual injury or a treat of an injury, in respect of an established domestic industry or injury significant enough to retard its establishment.

Causal link

With respect to determination of injury, it needs to be demonstrated that there is a causal relationship between the article that is alleged as being subsidized and the injury it seeks to cause to the domestic industry manufacturing or producing like product. In other words, it needs to be established that the injury to the domestic industry is consequent to import of subsidized article and not otherwise. If the injury is for reasons other than import of subsidized articles, then countervailing measures would not be imposed on the article.

Assessment of subsidy

The law does not decisively specify the manner in which the amount of subsidy given by another country is to be computed, but it contains certain guidelines for calculating the amount of subsidy under different circumstances including an illustrative list of certain kinds of subsidies. In this regard, the investigating authorities are expected to use analytical methods for consideration of these factors, which may be regarded as relevant in the light and circumstances of each case.

Guidelines for determination of subsidy

The following guidelines have been provided for the investigating authorities in calculating the amount of subsidy:

(a) Government provision of equity capital shall not be considered as conferring a benefit, unless the investment decision can be regarded as inconsistent with the usual investment practice (including for the provision of risk capital) of private investors in the territory of that Member;

(b) Loan given by the Government shall not be considered as conferring a benefit, unless there is a difference between the amount that the firm receiving the loan pays on the Government loan and the amount the firm would pay on a comparable commercial loan which the firm could actually obtain on the market. In this case the benefit shall be the difference between these two amounts;

(c) Loan guarantee given by the Government shall not be considered as conferring a benefit, unless there is a difference between the amount that the firm receiving the guarantee pays on a loan guaranteed by the Government and the amount that the firm would pay on a comparable commercial loan absent the Government guarantee. In this case the benefit shall be the difference between these two amounts adjusted for any differences in fees;

(d) The provision of goods or services or purchase of goods by a Government shall not be considered as conferring a benefit unless the provision is made for less than adequate remuneration, or the purchase is made for more than adequate remuneration. The adequacy of remuneration shall be determined in relation to prevailing market conditions for the good or service in question in the country of provision or purchase (including price, quality, availability, marketability, transportation and other conditions of purchase or sale).

Transition Rules and Special and Differential Treatment

1. Developed countries: Members not otherwise eligible for special and differential treatment are allowed three years from the date on which for them the SCM Agreement enters into force to phase out prohibited subsidies. Such subsidies must be notified within 90 days of the entry into force of the WTO Agreement for the notifying Member.

2. Developing countries: The SCM Agreement recognizes three categories of developing country Members: least-developed Members ("LDCs"), Members with a GNP per capita of less than $1000 per year which are listed in Annex VII to the SCM Agreement, and other developing countries. The lower a Member's level of development, the more favourable the treatment it receives with respect to subsidies disciplines. Thus, for example, LDCs and Members with a GNP per capita of less than $1000 per year listed in Annex VII are exempted from the prohibition on export subsidies. Other developing country Members have an eight-year period to phase out their export subsidies (they cannot increase the level of their export subsidies during this period). With respect to import-substitution subsidies, LDCs have eight years and other developing country Members five years, to phase out such subsidies. There is also more favourable treatment with respect to actionable subsidies. For example, certain subsidies related to developing country Members' privatization programmes are not actionable multilaterally.. With respect to countervailing measures, developing country Members' exporters are entitled to more favourable treatment with respect to the termination of investigations where the level of subsidization or volume of imports is small.

3. Members in transformation to a market economy: Members in transformation to a market economy are given a seven-year period to phase out prohibited subsidies. These subsidies must, however, have been notified within two years of the date of entry into force of the WTO Agreement (i.e., by 31 December 1996) in order to benefit from the special treatment. Members in transformation also receive preferential treatment with respect to actionable subsidies.

Notification

Subsidies Article 25 of the SCM Agreement requires that Members notify all specific subsidies (at all levels of government and covering all goods sectors, including agriculture) to the SCM Committee. New and full notifications are due every three years with update notifications in intervening years. The notifications are the subject of extensive review and discussion by the SCM Committee.

Countervailing legislation and measures

All Members are required to notify their countervailing duty laws and regulations to the SCM Committee pursuant to Article 32.6 of the SCM Agreement. Members are also required to notify all countervailing actions taken on a semi-annual basis, and preliminary and final countervailing actions at the time they are taken. Members also are required to notify which of their authorities are competent to initiate and conduct countervailing investigations.

Dispute Settlement

The SCM Agreement generally relies on the dispute settlement rules of the DSU. However the Agreement contains extensive special or additional dispute settlement rules and procedures providing, inter alia, for expedited procedures, particularly in the case of prohibited subsidy allegations. It also provides special mechanisms for the gathering of information necessary to assess the existence of serious prejudice in actionable subsidy cases

Procedural Matters

Making an application for investigation into countervailing measures

The investigations against alleged subsidy is normally initiated on the basis of a written request submitted "by or on behalf of" a domestic industry when domestic producers expressly supporting the application account for less than 25% of total production of the like product produced. However, the application would be considered to have been made "by or on behalf of the domestic industry" if it is supported by those domestic producers whose collective output constitutes more than 50% of the total production of the like product produced by that portion in the domestic industry, either expressing supporting or opposing the application.

The Application is required to include evidence of

(a) subsidy, and if possible, its amount,

(b) injury within the meaning of Article XVI of GATT 1994 and

(c) the causal link between the subsidized imports and its alleged injury. Further, the application should submit reasonable evidence and it should not be a simple assertion or of evidence, that is unsubstantiated.

Contents of the application

The application is required to contain the following information, for consideration by the investigation authorities:

(i) the identity of the applicant and a description of the volume and value of the domestic production of the like product by the applicant. Where a written application is made on behalf of the domestic industry, the application shall identify the industry on behalf of which the application is made by a list of all known domestic producers of the like product (or associations of domestic producers of the like product) and, to the extent possible, a description of the volume and value of domestic production of the like product accounted for by such producers;

(ii) a complete description of the allegedly subsidized product, the names of the country or countries of origin or export in question, the identity of each known exporter or foreign producer and a list of known persons importing the product in question;

(iii) evidence with regard to the existence, amount and nature of the subsidy in question;

(iv) evidence that alleged injury to a domestic industry is caused by subsidized imports through the effects of the subsidies; this evidence includes information on the evolution of the volume of the allegedly subsidized imports, the effect of these imports on prices of the like product in the domestic market and the consequent impact of the imports on the domestic industry, as demonstrated by relevant factors and indices having a bearing on the state of the domestic industry.

Processing of the application by the investigation authority

On receipt of the application the investigating authorities would examine the accuracy and adequacy of the evidence provided for determining whether there is sufficient evidence to justify the initiation of an investigation. On being satisfied with the documents presented but before initiating the investigation, the investigating authorities would be required to notify the exporting country of its intended investigation.

Whether application from domestic industry is necessary to initiate investigation?

The investigating authorities can also initiate the investigation suo moto i.e. on their own, if they consider that that they have sufficient evidence of the existence of subsidy, its injury and the causal link.

Whether investigation is to be initiated in all cases?

In order to ensure that investigations without merit are not continued, it is provided that the investigation should be terminated immediately if it found that the amount of subsidy is less than 1%, ad valorem (for developing nations, it is 2%) or the volume of subsidized imports from a country or the actual or potential injury, is negligible (for imports from developing nations, the volume of imports should be less than 4% when taken individually or 9% when considered collectively).

Time-limit to conduct the investigation

In order to minimize the trade-disruptive effect of investigations, it is specified that the investigations should be completed within one year and in no case, more than 18 months after initiation of investigation.

Transparency in investigation process

In order to ensure that there is transparency in proceedings, the authorities are also required to disclose the information on which determinations are to be based, to all interested parties and to provide them with adequate

opportunity to make or provide their comments. In this regard, the term 'interested party' has been defined to include (i) an exporter or foreign producer or the importer of a product subject to investigation, or a trade or business association a majority of the members of which are producers, exporters or importers of such product; and (ii) a producer of the like product in the importing Member or a trade and business association a majority of the members of which produce the like product in the territory of the importing Member. The definition of 'interested party' is meant to be inclusive and not exhaustive.

Manner under which the investigation is conducted

The procedural matters are common for anti-dumping and anti-subsidy. Accordingly, the provisions with respect to the governing authority for conducting investigation, the procedure adopted by them for investigation, the procedure adopted for determination of the amount of countervailing duty, whether provisionally or finally, the persons authorized to represent, retrospective powers of the authority, the appeal provisions, etc., has already been covered in the section pertaining to antidumping and accordingly they have not been repeated herein.

LEGAL FRAMEWORK WITH RESPECT TO IMPOSITION OF ANTI-SUBSIDY IN INDIA

The provisions governing the levy of anti-subsidy duty or countervailing duty is contained in the Customs Tariff Act, 1975 and the Rules made thereunder. Section 9 of the Act, provides for levy and collection of countervailing duty on import of subsidized articles into India from a country outside India. The Customs Tariff (Identification, Assessment and Collection of Countervailing Duty on Subsidized Articles and for Determination of Injury) Rules, 1995, provide for rules to determine the manner in which the subsidized articles liable for countervailing duty are to be identified, the manner in which subsidy provided is to be determined and the manner in which the duty is to be collected and assessed under the Act. There are separate provisions providing for the circumstances under which the levy under Section 9 would not be applicable and the procedure for appeal. These are contained in Section 9B and Section 9C of the Act, respectively. Accordingly, Sections 9, 9B and

9C together with the Rules referred to above, contain the provisions governing Antisubsidy.

IMPLEMENTING AUTHORITIES IN INDIA

- In India the Designated Authority for anti dumping is also the Authority for administering anti subsidy countervailing measures.
- The antidumping & countervailing measures are administered in India by the Directorate General of Anti-dumping and Allied Duties which was set up on 13th April 1998.
- In exercise of the powers conferred by sub-section (7) of section 9and subsection (2) of section 9B of the Customs Tariff Act, 1975 (51 of 1975) the Central Government had notified Customs Tariff (Identification and Assessment and Collection of Countervailing Duty on Subsidized Articles and for Determination of Injury) Rules,1995.
- Rule 3 provides for the appointment of designated authority by Central Government by notification in the official Gazette. Government may appoint an officer not below the rank of a Joint Secretary to the Government of India or such other officer as it may think fit as the designated authority for the purpose of these rules.
- The Designated Authority is a quasi-judicial authority notified under the Customs Act, 1962. A senior level Joint Secretary and Director, four investigating officers and four costing officers assist the DGAD. Besides, there is a section under the DGAD headed by the Section-Officer to deal with the monitoring and coordination of die functioning of the DGAD.
- The Designated Authority's function is to conduct the anti-dumping and anti-subsidy/ countervailing duty investigations and make recommendations to the Central Government for imposition of anti-dumping or countervailing measures where appropriate.

- These duties are finally imposed/ levied (and collected) by the Department of Revenue, Ministry of Finance through a Notification.
- Thus, while the Directorate General of Anti Dumping and Allied Duties in the Department of Commerce recommends the antidumping/ countervailing duty, it is the Department of Revenue, Ministry of Finance, which actually levies the duties.
- An appeal, if any, against the order of determination or review thereof regarding the existence, degree and effect of any subsidy or dumping in relation to import of any article lies before the Customs, Excise & Service Tax Appellate Tribunal (CESTAT-formerly known as CEGAT) and thereafter to the Supreme Court of India. However, various High Courts of the country also hear these matters under their writ jurisdiction.
- CSETAT reviews final measures and is independent of administrative authorities. This is consistent with the WTO provision of independent tribunals for appeal against final determination and reviews. No appeal will lie against the preliminary findings of the Authority and the provisional duty imposed on the basis thereof. The appeal to the CEGAT should be filed within 90 days.

DOHA DEVELOPMENT ROUND

The Doha Development Round or Doha Development Agenda (DDA) is the current trade-negotiation round of the World Trade Organization (WTO) which commenced in November 2001. Its objective is to lower trade barriers around the world, which will help facilitate the increase of global trade. As of today, talks have stalled over a divide on major issues, such as agriculture, industrial tariffs and non-tariff barriers, services, and trade remedies. The most significant differences are between developed nations led by the European Union (EU), the United States (USA), and Japan and the major developing countries led and represented mainly by Brazil, China, India, South Korea, and South Africa. There is also considerable contention against and between the EU and the USA over their maintenance of agricultural subsidies which is seen to operate effectively as trade barriers.

The Doha Round began with a ministerial-level meeting in Doha, Qatar in 2001. Subsequent ministerial meetings took place in Cancún, Mexico (2003), and Hong Kong (2005). Related negotiations took place in Paris, France (2005), Potsdam, Germany (2007), and Geneva, Switzerland (2004, 2006, 2008); The July 2008 negotiations broke down after failing to reach a compromise on agricultural import rules. After the breakdown, major negotiations were not expected to resume until 2009. Nevertheless, intense negotiations, mostly between the USA, China, and India, were held in the end of 2008 in order to agree on negotiation modalities. The impasse was not resolved and, in April 2011, director-general Pascal Lamy "asked members to think hard about 'the consequences of throwing away ten years of solid multilateral work." Though no significant progress has eventuated from the negotiations, the WTO seems determined to persist with them. A report to the WTO General Council by Lamy in May 2012 advocated "small steps, gradually moving forward the parts of the Doha Round which were mature, and re-thinking those where greater differences remained."The Doha Round negotiations are still going on.

Doha Round talks are overseen by the Trade Negotiations Committee (TNC), whose chair is the WTO's director-general, currently Pascal Lamy. The negotiations are being held in five working groups and in other existing bodies of the WTO.

Before the Doha ministerial, negotiations had already been under way on trade in agriculture and trade in services. These ongoing negotiations had been required under the last round of multilateral trade negotiations (the Uruguay Round, 1986–1994). However, some countries, including the United States, wanted to expand the agriculture and services talks to allow trade-offs and thus achieve greater trade liberalization.

The first WTO ministerial conference, which was held in Singapore in 1996, established permanent working groups on four issues: transparency in government procurement, trade facilitation (customs issues), trade and investment, and trade and competition. These became known as the Singapore issues. These issues were

pushed at successive ministerial by the European Union, Japan and Korea, and opposed by most developing countries. Since no agreement was reached, the developed nations pushed that any new trade negotiations must include these issues.

The negotiations were intended to start at the ministerial conference of 1999 in Seattle, USA, and be called the Millennium Round but, due to several different events including protest activity outside the conference (the so-called "Battle of Seattle"), the negotiations were never started. Due to the failure of the Millennium Round, it was decided that negotiations would not start again until the next ministerial conference in 2001 in Doha, Qatar.

WTO Ministerial Conference of 2001 began in November 2001, committing all countries to negotiations opening agricultural and manufacturing markets, as well as trade-in-services (GATS) negotiations and expanded intellectual property regulation (TRIPS). The intent of the round, according to its proponents, was to make trade rules fairer for developing countries. More than 40 items under 12 headings were settled at or before the Doha conference in Nov 2001, for immediate delivery. The vast majority of the remaining items were subject of negotiations.

Developing countries claim that they have had problems with the implementation of the agreements reached in the earlier Uruguay Round because of limited capacity or lack of technical assistance. They also claim that they have not realized certain benefits that they expected from the Round, such as increased access for their textiles and apparel in developed-country markets. They seek a clarification of language relating to their interests in existing agreements.

Before the Doha ministerial, WTO members resolved a small number of these implementation issues. At the Doha meeting, the Ministerial Declaration directed a two-path approach for the large number of remaining issues: (a) where a specific negotiating mandate is provided, the relevant implementation issues will be addressed under that mandate; and (b) the other outstanding implementation issues will be addressed as a matter of priority by the relevant WTO bodies. Outstanding implementation issues are found in the area of market access, investment measures, safeguards, rules of origin, and subsidies and countervailing measures, among others.

Certain implementation-related issues and concerns were decided on the SCM Agreement. These are explained below:

- Normally, subsidies that require recipients to export are banned. But some developing countries are allowed to pay these subsidies. Developing countries whose GNP stays below US $1,000 per capita were exempted. The ministers agree that this threshold should be "US $1,000 in constant 1990 dollars for three consecutive years".
- The ministers also underscore that countries in this group will continue to be eligible "so long as its GNP per capita in current dollars has not reached US $1000 based upon the most recent data from the World Bank".
- The ministers agree that a country dropped from the list can be restored to the list if its GNP per capita drops below US$ 1,000.
- However question on how to calculate "constant 1990 dollars" is still pending for negotiations.
- Some subsidies in developing countries with "legitimate development goals", and include support for regional growth, technology research and development, production diversification, and development and implementation of environmentally sound methods of production should not face countervailing measures or other actions from other governments.
- Least-developed countries' "export competitiveness": The ministers affirm that least-developed countries' governments are allowed to pay subsidies that require recipients to export, normally prohibited, "and thus have flexibility to finance their exporters, consistent with their development needs".
- However, the least-developed countries that have "reached export competitiveness" in a product must phase out the subsidies on that product within eight years.

- "Export competitiveness" is 3.25% of world trade in a product, with some details about how that is to be demonstrated.
- More time for some developing countries to phase out export-contingent subsidies was provided.

Agriculture has become the most important and controversial issue. Agriculture is particularly important for developing countries, because around 75% of the population in developing countries live in rural areas, and the vast majority are dependent on agriculture for their livelihoods. The first proposal in Qatar, in 2001, called for the end agreement to commit to substantial improvements in market access; reductions (and ultimate elimination) of all forms of export subsidies; and substantial reductions in trade-distorting support."The United States is being asked by the European Union (EU) and the developing countries, led by Brazil and India, to make a more generous offer for reducing trade-distorting domestic support for agriculture. The United States is insisting that the EU and the developing countries agree to make more substantial reductions in tariffs and to limit the number of import-sensitive and special products that would be exempt from cuts. Import-sensitive products are of most concern to developed countries like the European Union, while developing countries are concerned with special products – those exempt from both tariff cuts and subsidy reductions because of development, food security, or livelihood considerations. Brazil has emphasized reductions in trade-distorting domestic subsidies, especially by the United States (some of which it successfully challenged in the WTO U.S.-Brazil cotton dispute), while India has insisted on a large number of special products that would not be exposed to wider market opening.

It is concede by all the countries that subsidies need to be reduced and should be ultimately phased out in agriculture. However in the case of food security concerns, exception is permitted. All forms of export subsidies will be phased out. This is big problem for developed countries which have been providing mounting subsidies.

CASE STUDY - INDIA'S EXPORT SUBSIDIES ON TEXTILES

Subsidies Committee of World Trade Organisation encourages members to notify their subsidy programmes. The Committee has reviewed notifications of new countervailing duty legislation of the following members: United States, Tonga and Burkina Faso.

The United States has tabled a proposal for defining time limits to answer written requests by members on the nature and extent of subsidies granted by other members. Australia, EU and Canada expressed general support for the US proposal while some other members said they needed to study it further.

The United States has called on China and India to notify 200 and 50 subsidy programmes, respectively, to the Committee following the counter-notification made by the US under Article 25.10 of the Subsidies Agreement. It said that most of these subsidy programmes, which included a number of programmes of local governments, were not included in the most recent subsidy notifications of these two countries. The EU, Canada, Japan, Norway and Turkey shared the US concerns. China reiterated that the United States continued to have a lot of misunderstanding about its subsidy programmes, adding that a number of programmes in the US list were already covered in China's notification to the Committee. India said many of its programmes listed by the US are not prohibited by the Subsidies Agreement, and cited an infrastructure programme as an example. The United States said it would be willing to discuss these matters further with China and India.

The Committee on Subsidies and Countervailing Measures, on 23 October 2012, approved the final extension of the transition period — until end 2013 — for export subsidy programmes of 19 developing countries. These programmes consist mainly of free trade zones and tax incentives.

Textile export is important for India's economy as the sector is the largest job provider in the country. With the downturn in global trade reducing demand for exports, the Government has been providing several incentives to exporters. In December 2012, the Government of India had announced extension of two percent interest subsidy on some labour-intensive industries, including textiles, garments and handicrafts, for one more year till March 2014. The decision to extend the interest subvention scheme was taken in view of the country's overall exports falling by 5.95 percent year-on-year to US$ 189 billion during the first eight months of 2012 -

2013. The step was taken to reduce the country's trade deficit. India's exports of readymade garments, carpets and jute products declined by 8 percent, 11 percent and 14 percent respectively, during the April-November period of 2012. The Minister also announced extension of two percent interest subsidy on incremental exports that would be achieved during January-March 2013 over the period January-March 2012.

However, the United States and Turkey called on India to stop extending export subsidies to its textile and apparel industry, and to phase-out its existing subsidy programmes as required by the Subsidies Agreement for developing countries that have attained export competitiveness in a particular sector. Turkey said that subsidized Indian textile producers posed unfair competition to its producers. The United States, which recalled that it was the one that had asked the WTO Secretariat to calculate India's competitiveness in the textile and apparel sector, said that it was concerned that with new programmes, India seemed to have gone in the opposite direction in fulfilling its subsidy obligations.

Pressure is mounting on India at the World Trade Organisation (WTO) to pare subsidies and incentives given to its textiles sector. The European Union and Japan have joined hands with the US and Turkey to demand that India stop giving fresh subsidies and gradually phase out the existing ones as the textiles sector had already achieved export competitiveness.

The WTO allows countries with per capita income below $1,000 to give export subsidies till exports are lower than 3.25 per cent of world trade in that particular commodity. India's share in the global market for textiles crossed the limit in 2007, according to WTO records, and is almost four per cent at the moment. Since countries are given eight years to remove the subsidies, India has time till 2015 to do so. "There is also no clarity over whether India actually crossed the threshold in 2007. We have to reach an agreement even on this," the official said.

India, however, maintains that many of the subsidies identified by the US and others are not subsidies and merely a reimbursement of input duties. It said before the phasing out happens, there has to be a common understanding on what the subsidies are, definition of products covered, and when should the phase-out begin. The issue came up for discussion at a recent meeting of the WTO Committee on Subsidies and Countervailing Measures. India is prepared to work with the Committee and interested members on this issue.

Read the case and examine whether India should stop providing subsidy to textile sector?

Hints:

- India maintains that many of the subsidies identified by the US and others are not subsidies and merely a reimbursement of input duties.
- In the WTO negotiations developed countries want some prominent developing nations like India, China and Brazil to take commitments of complete duty elimination in specific sectors. However, India has reservations on account of the effect of such a commitment on sectors and products which are critical for employment generation and economic growth. Textile export is important for India's economy as the sector is the largest job provider in the country.
- India should raise concerns relating to the unfair trade practices and policies being followed by the US which have an effect on India's exports like exorbitantly high countervailing duty imposed on Indian steel products, and the US policy of giving preference to their domestic solar energy equipment manufacturers for availing subsidy, thereby discriminating against imported products.

LESSON ROUND UP

- In common parlance, the term subsidy means money granted by the State or a Public Body to keep the prices of commodities under control. Subsidy may take the form of direct or indirect government grants on production or exportation of goods including any special subsidy on transportation of any product.
- The Agreement on Subsidies and Countervailing Measures ("SCM Agreement") addresses two separate but closely related topics: multilateral disciplines regulating the provision of subsidies, and the use of countervailing measures to offset injury caused by subsidized imports.
- The SCM Agreement creates two basic categories of subsidies: prohibited and actionable (*i.e.,* subject to challenge in the WTO or to countervailing measures). All specific subsidies fall into one of these two categories.
- A determination of injury is based on positive evidence and involve an objective examination of both
  (a) the volume of the subsidized imports and the effect of the subsidized imports on prices in the domestic market for like products; and
  (b) the consequent impact of these imports on the domestic producers of such products.

SELF TEST QUESTIONS

1. What do you mean by subsidy and countervailing duty? Compare and contrast anti dumping duty and countervailing duty.
2. 'The SCM Agreement creates two basic categories of subsidies'. Explain briefly.
3. What are the types of 'specificity' that come within the ambit of SCM Agreement?
4. Write a note on the designated authority for Anti subsidies in India.
5. Briefly discuss the procedure for making an application for investigation into countervailing measures under SCM Agreement.

Lesson 10
Foreign Collaborations and Joint Ventures

LESSON OUTLINE

- Foreign collaboration
- Features of foreign collaboration
- Objectives of foreign collaboration
- Types of foreign collaboration
- Joint venture
- Reasons for forming a joint venture
- Basic elements of a joint venture
- Structuring the joint venture
- Managing the joint venture
- Modes of joint venture
- Advantages of joint venture
- Disadvantages of joint venture
- Termination of joint ventures
- Examples of joint ventures
- Joint venture agreements
- Drafting of a joint venture agreement
- Specimen joint venture agreement
- International commercial arbitration
- Benefits of international commercial arbitration
- Examples of some arbitration clause
- Case study
- LESSON ROUND UP
- SELF TEST QUENSTIONS

LEARNING OBJECTIVES

Foreign collaborations or joint ventures are one of the most prominent modes of entry into the global markets. Joint ventures are being set up in today's economic world by both the public and private sector companies. Many Indian companies have set up joint ventures in developing countries like Malaysia, Indonesia, Singapore, Sri-Lanka, Nigeria, Thailand etc.

Joint venture is a shared ownership in foreign business. It is generally short lived for conducting specific business activities. A joint venture (JV) is a business agreement in which the parties agree to develop, for a finite time, a new entity and new assets by contributing equity. They exercise control over the enterprise and consequently share revenues, expenses and assets. There are other types of companies such as joint ventures limited by guarantee, joint ventures limited by guarantee with partners holding shares.

Since money is involved in a joint venture, it is necessary to have a strategic plan in place. In short, both parties must be committed to focusing on the future of the partnership, rather than just the immediate returns.

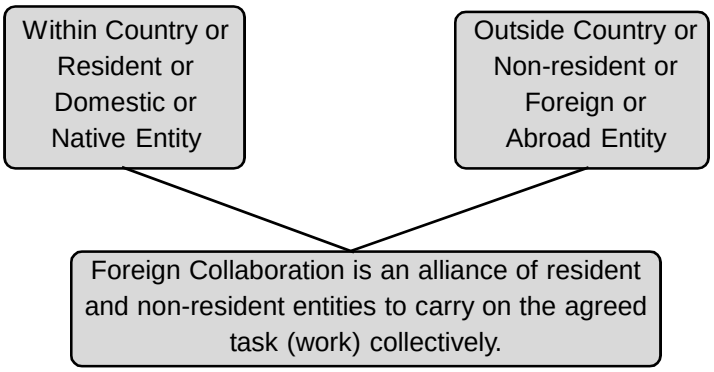
In this chapter we will discuss about foreign collaborations types joint ventures, types of ventures, how to enter into ventures, preparing agreement and finally about the arbitration as a tool of dispute settlement.

"If you do not seek out allies and helpers, then you will be isolated and weak." Sun Tzu, "The Art of War"

"You can adapt by changing your organization's relationships with other organizations through corporate partnerings. Instead of building internal capabilities you turn to partnerships and alliances. As you need to change and adapt, you change partners. Companies that know how to form and use these partnerings are displacing those that don't get it." Curtis E. Sahakian

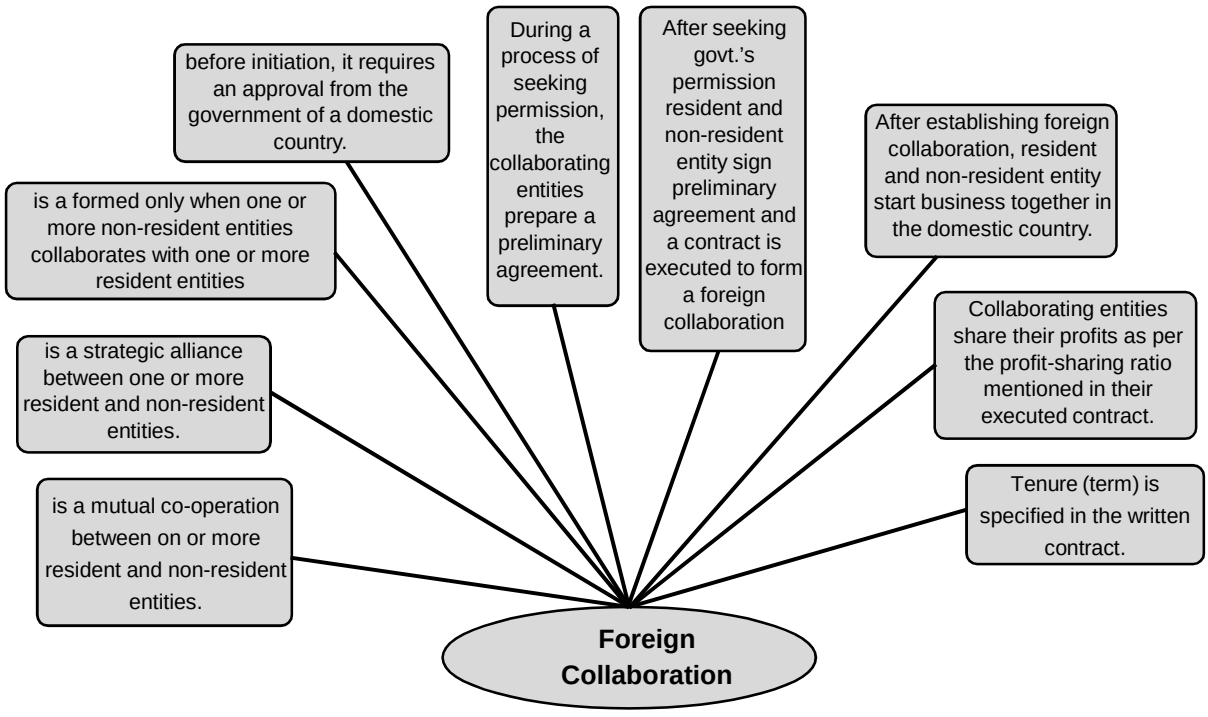
FOREIGN COLLABORATION

"Foreign collaboration is an alliance incorporated to carry on the agreed task collectively with the participation (role) of resident and non-resident entities." Foreign collaboration is an alliance of domestic (native) and foreign (non-native) entities like individuals, firms, companies, organizations, governments, etc., that come together with an intention to finalize a contract on some tasks or jobs or projects.



In finance, the definition of foreign collaboration can be specified as follows. "Foreign collaboration includes ongoing business activities of sharing information related to financing, technology, engineering, management consultancy, logistics, marketing, etc., which are generally, offered by a non-resident (foreign) entity to a resident (domestic or native) entity in exchange of cheap skilled and semi-skilled labour, inexpensive high-quality raw-materials, low cost hi-tech infrastructure facilities, strategic (favourable) geographic location, and so on, with an approval (permission) from a governmental authority like the ministry of finance of a resident country."

Foreign collaboration is thus an alliance (a union or an association) formed for mutual benefit of collaborating parties. The meaning of foreign collaboration is depicted in the following chart.



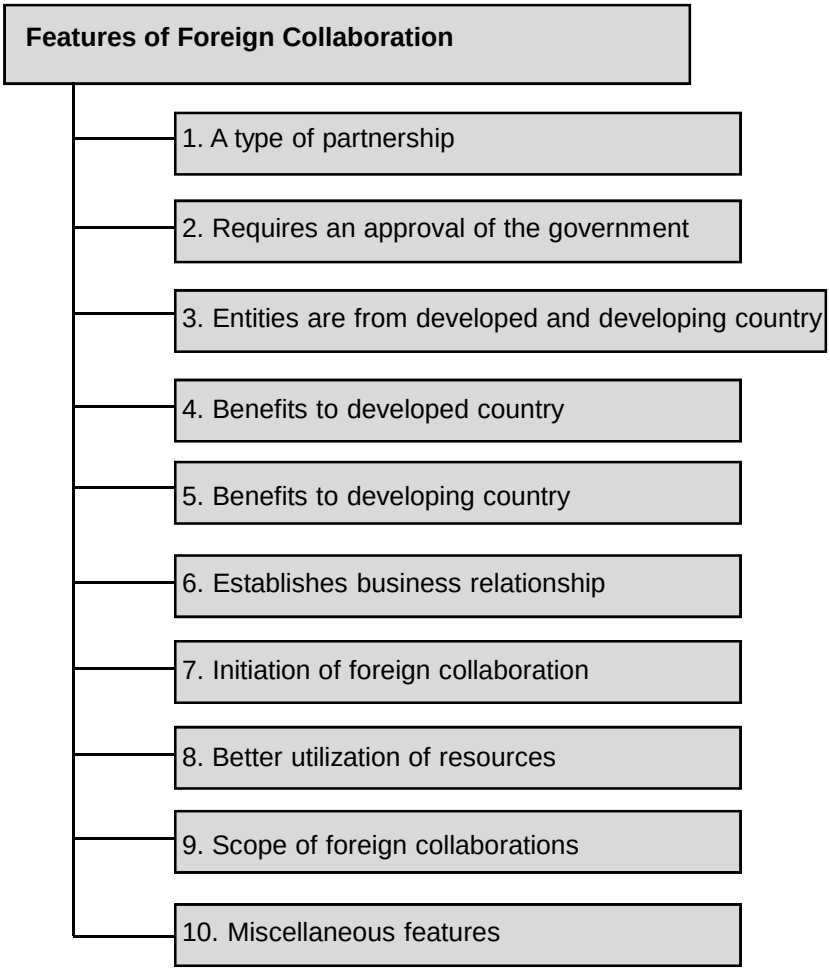
- Foreign collaboration is a mutual co-operation between one or more resident and non-resident entities. In other words, for example, an alliance (a union or an association) between a foreign based company and a domestic company forms a foreign collaboration. It is a strategic alliance between one or more resident and non-resident entities. Only two or more resident (native) entities cannot make a foreign collaboration possible. For its formation and as per above definitions, it is mandatory that one or more non-resident (foreign) entities must always collaborate with one or more resident (domestic) entities.
- Before starting a foreign collaboration, both entities, for example, a resident and non-resident company must always seek approval (permission) from the governmental authority of the domestic country.
- During an ongoing process of seeking permission, the collaborating entities prepare a preliminary agreement.
- According to this preliminary agreement, for example, the non-resident company agrees to provide finance, technology, machinery, know-how, management consultancy, technical experts, and so on. On the other hand, resident company promises to supply cheap labour, low-cost and quality raw-materials, sufficient land for setting factories, etc.
- After obtaining the necessary permission, individual representative of a resident and non-resident entity signs this preliminary agreement. Signing the agreement acts as a written acceptance to each other's expectations, terms and conditions. After accptance, a contract is executed, and foreign collaboration gets established. Contract is a legally enforceable agreement.
- After establishing foreign collaboration, resident and non-resident entity start business together in the domestic country.
- Collaborating entities share their profits as per the profit-sharing ratio mentioned in their executed contract.
- The tenure (term) of the foreign collaboration is specified in the written contract.

Examples of Foreign Collaboration

Some prominent examples of foreign collaboration between an Indian and Foreign entity are depicted below.

- ICICI Lombard GIC (General Insurance Company) Limited is a financial foreign collaboration between ICICI Bank Ltd., India and Fairfax Financial Holdings Ltd., Canada.
- ING Vysya Bank Ltd. is a financial foreign collaboration formed between ING Group from Netherlands and Vysya Bank from India.
- Tata DOCOMO is a technical foreign collaboration between Tata Teleservices from India and NTT Docomo, Inc. from Japan.
- Sikkim Manipal University (SMU) from India runs some academic programs through an educational foreign collaboration with abroad universities like Liverpool School of Tropical Medicine from UK, Loma Linda and Louisiana State Universities from USA, Kuopio University from Finland, and University of Adelaide from Australia.

FEATURES OF FOREIGN COLLABORATION



1. **A type of partnership:** Foreign collaboration is a type of partnership between a domestic entity and foreign based entity. In such an alliance, each partner plays some crucial role. Foreign entity generally provides support for finance, technology, engineering, management, etc. On the other hand, a domestic based entity provides cheap labour, high-quality raw materials, land and so on. Here, domestic and foreign entity share their profits as per profit-sharing ratio mentioned in their contract.
2. **Requires an approval of the government:** Before initiating foreign collaboration, collaborating entities (domestic and foreign) must seek permission from the government of the domestic country. The government gives approval only when the contract of foreign collaboration is prepared in accordance with the industrial or foreign policy of its country.
3. **Entities are from developed and developing country:** In foreign collaboration, one or more abroad entities are generally from developed countries like U.S.A., Germany, Japan, etc. Whereas, a domestic entity is from a developing country or less-developed country (LDC). Some examples of developing countries are India, Sri-Lanka, Indonesia, and so on.
4. **Benefits to developed country:** The benefits of foreign collaboration to a developed country are as follows:
   - Foreign collaboration helps a developed country earn good returns on its overall investments made in a domestic country.
   - It also aids a developed country earn a good reputation for providing financial and technical assistance (support) to the developing country.

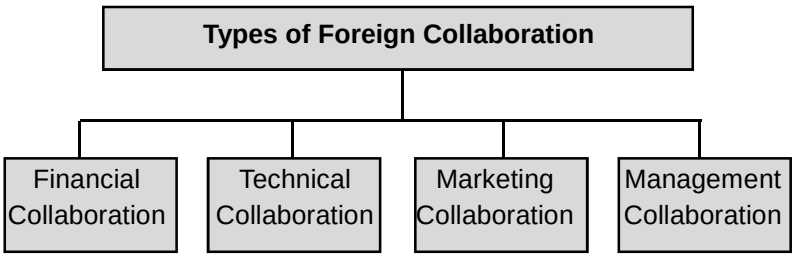
5. **Benefits to developing country:** The benefits of foreign collaboration to a developing country are as follows:
   - Foreign collaboration helps a developing country to get finance, technology, machinery, know-how, management and technical expertise, etc. from a developed country.
   - It also assists a developing country to achieve a faster economic growth.
6. **Establishes business relationships:** Foreign collaboration establishes business (trade) relationships among different countries. It removes their economic gaps (hurdles) and brings them closer to each other.
7. **Initiation of foreign collaboration:** A foreign collaboration is initiated at the government and/or corporate level. At governmental level foreign collaboration, a government of some foreign country collaborates with the government of a domestic country. Similarly, at corporate level foreign collaboration, a company from some foreign country collaborates with the company from a domestic country. These companies may be either private or public in nature.
8. **Better utilization of resources:** Though developed countries are good with finance, technology, management and technical expertise, generally, they face difficulties to meet a continuous supply of low-cost labour and quality raw materials. On the other hand, generally, a developing country has more availability of low-cost labour and plenty of quality raw materials. Foreign collaboration brings developed and developing country together and helps them to satisfy each other's needs by exchanging their excess resources. Finally, this leads to a better utilization of available resources.
9. **Scope of foreign collaboration:** The scope of foreign collaboration is very wide. It covers core business activities such as: Finance, Production, Management and Technical consultancy, Advertising and Marketing, etc.
10. **Miscellaneous features:** Miscellaneous features of foreign collaboration are listed as follows:
    - Foreign collaboration reduces unemployment in a developing country.
    - It improves infrastructure in a developing country.
    - It helps to increase revenue of the governments in the form of taxes and duties.
    - It also aids to achieve economic growth in developed and developing country.

OBJECTIVES OF FOREIGN COLLABORATION

The main intention or prime goal or objective of foreign collaboration is to:

- Improve the financial growth of the collaborating entities.
- Occupy a major market share for the collaborating entities.
- Reduce the higher operating cost of a non-resident entity.
- Make an optimum and effective use of resources available in the resident entity's country.
- Generate employment in the resident entity's country.

TYPES OF FOREIGN COLLABORATION



1. **Financial collaboration:** In case of financial collaboration, the inflow of foreign investment takes place in the domestic (host) country. In this method, the foreign company lends finance by:
   - ***Purchasing ownership shares:*** Here, foreign company purchases ownership shares of the domestic company and in return gets the dividend for these shares.
   - ***Giving long-term loans:*** Here, foreign company gives long-term loans to the domestic company and in return gets interest from these loans.
   - ***Giving credit facility:*** Here, foreign company gives credit facility to the domestic (native) company. The native company uses this credit facility to purchase raw-materials, plant and machinery.

   Thus, in financial collaboration, there is an inflow of finance from developed countries to developing countries.
2. **Technical collaboration:** In case of technical collaboration, the inflow of foreign technology takes place in the domestic (host) country. Technical collaboration includes integration of foreign technology with domestic (indigenous) technology. In technical collaboration, the foreign company provides technological know-how, professional services and expertise, installs automated machineries, etc., in the domestic country. Here, an inflow of modern technology takes place from the developed country to the developing country. Technical collaboration helps to remove an existing technological gap. Therefore, the governments of developing countries encourage such collaborations. In developing countries, most of the foreign collaborations are technical in nature.
3. **Marketing collaboration:** In case of marketing collaboration, the inflow of foreign goods and services take place in the domestic (host) country. In marketing collaboration integration of domestic and foreign market takes place. In marketing collaboration, foreign company agrees to sell goods produced by the domestic company. The foreign company sells these goods in its own country and/or in the international market. It uses its distribution network to sell the goods. From the viewpoint of a developing country, marketing collaboration is very beneficial for increasing its exports of goods and services.
4. **Management consultancy collaboration:** In case of management consultancy collaboration, the inflow of foreign management consultancy takes place in the domestic (host) country. In management consultancy collaboration integration of domestic and foreign consultancy takes place.In management consultancy collaboration, foreign company provides management skills to the domestic company and teaches it everything about management. In other words, it gives advice and solves management problems of the domestic company. It teaches management skills for the following:
   - Production management.
   - Marketing management.
   - Personnel management.
   - Financial management.

   The foreign company also helps the domestic company to modernize and diversify its business process. So, in management consultancy collaboration, the foreign company increases the management efficiency of the domestic company. This type of collaboration is found in both private and public sector.

JOINT VENTURE

As business projects get larger, technology more expensive, and the costs of failure too large to be borne alone, businesses feel the need to work with joint ventures. In general, a joint venture ("JV") is an association of two or more entities (whether corporate, government, individual or otherwise) combining property and expertise to carry out a single business enterprise and having a joint proprietary interest, a joint right to control and a sharing of profits and losses.

Regardless of the scope of the undertaking, the nature of the JV or the respective degrees of equity or management involvement, a JV must:

- be a separately identifiable entity;
- have an ownership interest in such entity by each joint venture partner ("JVP"); and
- have an active management involvement or deliberate rejection of the right to such involvement by each JVP.

A joint venture is an association of two or more individuals or business entities who combine and pool their respective expertise, financial resources, skills, experience, and knowledge in the furtherance of a particular project or undertaking. Joint Ventures are generally created for a single activity or project, and may have a limited time span. Joint Venture agreements, commonly referred to as a "JV", are typically formed either by individuals, business entities, corporations or partnerships. The contributions to the joint ventures are either in the form of money [capital], services, or physical asset(s), i.e. equipment or intellectual property [software, patents], etc., or a combination of all.

The joint ventures utilize a separate business entity to conduct the specified business activities. The use of a separate entity allows the parties to limit the liabilities associated with the relationship. More precisely, a joint venture is required in order for the parties to avail themselves of incentives and concessions offered under any local foreign investment programmers.In essence, a joint venture arrangement consists of an agreement between two or more parties to combine, in a specific way, a certain kind or amount of their resources in order to manufacture, produce or sell a product or to render a service and share in a specified manner the profits that result and the risks that occur.

The rationale for joint venture varies from case to case according to the strategic business objectives and capacity of the individual partners, as well as external factors. They are often the means of acquiring raw materials, production facilities, technology or know-how. Most often, however, they are the means of expanding into new markets. Market access may, for instance, depend on linking up with established distribution channels or operating under a brand name already well recognized in the market place. The risks of operating in an unfamiliar jurisdiction can be daunting, but the management of these risks can be enhanced by a joint venture with a compatible local partner familiar with local business practices, processes, procedures, laws and customs.

In increasing numbers, businesses have been reaching beyond national boundaries in an effort to locate new opportunities for growth, new markets, and new venture capital. Each foreign market offers unique opportunities and risks, and many firms naturally look to JVs with one or more partners for assistance in entering new markets. JVs have become a major feature of the international business landscape due to increased global competitiveness and technological innovation.

An international joint venture is often described as the joining together of two or more business partners from separate jurisdictions to exchange resources, share risks and divide rewards from a joint enterprise. Usually, but not always, one of the partners is physically located in the jurisdiction of the joint venture. An IJV has elements of a partnership, but is typically formed for a defined purpose or specified project, and, therefore, is usually limited in purpose, scope and duration. The contributions of the joint venture partners often differ and tend to be specified based on the capabilities of each partner and the nature of the venture. Although legal agreements are required to create and sustain international joint ventures, in order to prosper, IJVs must be practical, living and evolving relationships. Continued positive interaction and dialogue between the business decision-makers after the formation of the joint venture is critical. Circumstances change and the management team and the joint venture itself must be capable of changing with them.

International JVs are those in which one of more or the parties is located outside the domestic boundary of that country or those in which the operations of the JV take place, or are directed toward, territories abroad. About three-quarters of all JVs are international. Many countries have created a wide range of economic incentives for using a JV structure for foreign investment. Because such arrangements necessarily involve two or more sovereign jurisdictions, international JVs present special problems. The international JV must consider the host country's investment laws and regulations and often obtain the host country's governmental approval.

JVs are common and successful in several industries. For example, in the land development and construction industries, JVs are often used to obtain sufficient financing to acquire large land tracts or to undertake major building projects. JVs are also common in the manufacturing, mining, and service industries. A JV may be formed to conduct research and development work on a new product or technical application, to manufacture or produce various products, to market and distribute products and services in a specified geographic area, or to perform a combination of these functions. The function of the JV will be linked to the overall objectives of the parties and will dictate to a large extent the substantive terms of the JV arrangement.

The formation of a JV can be a complex process. After a compatible JVP is selected, the specific goals of the enterprise must be defined, the structure of the JV must be negotiated, numerous legal issues must be recognized and resolved, and potential areas of conflict between the JVPs must be identified and reconciled.

REASONS FOR FORMING A JOINT VENTURE

There are many motivations that lead to the formation of a JV. They include:

(a) Risk Sharing : Risk sharing is a common reason to form a JV, particularly, in highly capital intensive industries and in industries where the high costs of product development equal a high likelihood of failure of any particular product.

(b) Economies of Scale : If an industry has high fixed costs, a JV with a larger company can provide the economies of scale necessary to compete globally and can be an effective way by which two companies can pool resources and achieve critical mass.

(c) Market Access : For companies that lack a basic understanding of customers and the relationship/ infrastructure to distribute their products to customers, forming a JV with the right partner can provide instant access to established, efficient and effective distribution channels and receptive customer bases. This is important to a company because creating new distribution channels and identifying new customer bases can be extremely difficult, time consuming and expensive activities.

(d) Geographical Constraints : When there is an attractive business opportunity in a foreign market, partnering with a local company is attractive to a foreign company because penetrating a foreign market can be difficult both because of a lack of experience in such market and local barriers to foreign-owned or foreign-controlled companies.

(e) Funding Constraints : When a company is confronted with high up-front development costs, finding the right JVP can provide necessary financing and credibility with third parties.

(f) Acquisition Barriers Prelude to Acquisition : When a company wants to acquire another but cannot due to cost, size, or geographical restrictions or legal barriers, teaming up with a JVP is an attractive option. The JV is substantially less costly and thus less risky than complete acquisitions, and is sometimes used as a first step to a complete acquisition with the JVP. Such an arrangement allows the purchaser the flexibility to cut its losses if the investment proves less fruitful than anticipated or to acquire the remainder of the company under certain circumstances.

BASIC ELEMENTS OF A JOINT VENTURE

(a) Contractual Agreement : JVs are established by express contracts that consist of one or more agreements involving two or more individuals or organizations and that are entered into for a specific business purpose.

(b) Specific Limited Purpose and Duration : JVs are formed for a specific business objective and can have a limited life span or it can be long-term. JVs are frequently established for a limited duration because (a) the complementary activities involve a limited amount of assets; (b) the complementary assets have only a limited service life; and/or (c) the complementary production activities will be of only limited efficacy.

(c) Joint Property Interest : Each JV participant contributes property, cash, or other assets and organizational capital for the pursuit of a common and specific business purpose. Thus, a JV is not merely a contractual relationship, but rather the contributions are made to a newly-formed business enterprise, usually a corporation, limited liability company, or partnership. As such, the participants acquire a joint property interest in the assets and subject matter of the JV.

(d) Common Financial and Intangible Goals and Objectives : The JV participants share a common expectation regarding the nature and amount of the expected financial and intangible goals and objectives of the JV. The goals and objectives of a JV tend to be narrowly focused, recognizing that the assets deployed by each participant represent only a portion of the overall resource base.

(e) Shared Profits, Losses, Management, and Control : The JV participants share in the specific and identifiable financial and intangible profits and losses, as well as in certain elements of the management and control of the JV.

STRUCTURING THE JOINT VENTURE

Structuring a Joint Venture is a difficult task. It is especially true where parties are from different jurisdictions and various cultural backgrounds are involved. After parties have decided on fundamental issues such as the commercial nature, scope and mutual objectives of the joint venture, the JVPs must determine the geographic location of the venture and what form or legal structure the joint venture will take.

Generally, the structure chosen will be between different types of partnerships, corporations, or some form of a limited liability company, depending on the tax liability each JVP wants to be exposed to. The tax and legal features of types of JV will vary from one country to another. Some of the forms of JV are as follows:

(a) Corporations : Corporations are a commonly preferred choice for JVs. The legal status of a corporation is clear, and its ability to own assets, incur liabilities and enter into legally binding contracts is obvious to third parties. The liability of shareholders for the corporation's debts and obligations is limited to their capital investment in the corporation. From a tax perspective, corporations may be undesirable because they generally lack pass-through tax status, making its shareholders unable to set off profits and losses generated by the JV against income or expenses from other activities. Also, the net income of a corporation is likely to be subject to corporate tax in the jurisdiction it is located. Such tax payable by the corporation may not be credible against taxes payable on dividends and other profit distribution from the corporation and its shareholders. However, the presence or absence of tax treaties between respective countries may make the corporation profitable.

(b) General Partnerships : All partners in a general partnership have personal liability for debts and other obligations incurred by the partnership. One advantage of a general partnership in many countries is that normally tax imposed is less on it. Also, all partners can act on behalf of, and legally bind, the partnership via third parties.

(c) Limited Partnerships : Under a limited partnership there are two distinct types of partners, general and limited. The general partner carries responsibilities similar to the one he carries in a general partnership, including the ability to legally bind the whole partnership and being personally liable for debts and obligations of the partnership. The limited partner, on the other hand, mainly contributes capital and receives a specified share of the profits. The limited partner is excluded from active management of the partnership, but is exempt from personal liability for debts and obligations of the partnership.

(d) Limited Liability Company (LLC) or Limited Liability Partnership (LLP) : A limited liability company is a hybrid between the partnership and the corporation. It provides the JVPs with insulation from the liabilities of the LLP/LLC in a corporation, while generally being classified as a partnership for tax purposes. All members may take part in management. Hybrid vehicles such as the LLC/LLP are not recognized in all parts of the world.

MANAGING THE JOINT VENTURE

Some JVs are *dominant parent* enterprises – projects are managed by one parent like wholly owned subsidiaries. The dominant parent selects all the functional managers for the enterprise. The board of directors, although made up of executives from each parent, plays a largely ceremonial role as the dominant parent executives make all the venture's operating and strategic decisions. Having managers from only one parent can lead to frustrations for the managers as well as parent company executives.

A dominant parent enterprise is appropriate where a JVP is chosen for reasons other than managerial input – i.e., financial backing, access to resources, patents, or because it consumes a large amount of the product to be made. Dominant parent joint ventures are also appropriate when a company takes on a partner solely in response to pressures from a host government. In such situations, a foreign company often prefers to find a passive local company that (1) has no knowledge of the product, (2) is willing to be a passive investor, and (3) is neither a government agency nor controlled by the government. The passive partner, who may be supplying technology or money, must trust the competence and honesty of the dominant parent. If the local partner never learns the business of the JV, the dominant parent's bargaining position with the host government will remain strong.

Other JVs are *shared management* ventures, where both parents manage the enterprise. Each parent supplies both functional managers and executives to serve on the board of directors. Here, the board of directors has a real decision-making function.

One type of shared management venture is the 50:50 JV. This type of JV is characterized by 50:50 participation in which each partner contributes 50 percent of the equity in return for 50 percent participating control. Under such participation, each JVP is at equal risk.

All shared management ventures own equal shares. JVs are flexible so that they can be structured in such as way that one JVP has more than a co-equal role in the JV (e.g., 40/60).

Shared management is critical in ventures where both JVPs are needed for managerial input, as in manufacturing situations where one parent is supplying technology and the other knowledge of the local market. However, deteriorating performance in a shared management venture obliges each parent to become more involved in the operation of the venture. Unless either parent is willing to defer to the other's knowledge or expertise, the decision-making process can become slow can confused and trigger a series of events that can lead to the destruction of the venture.

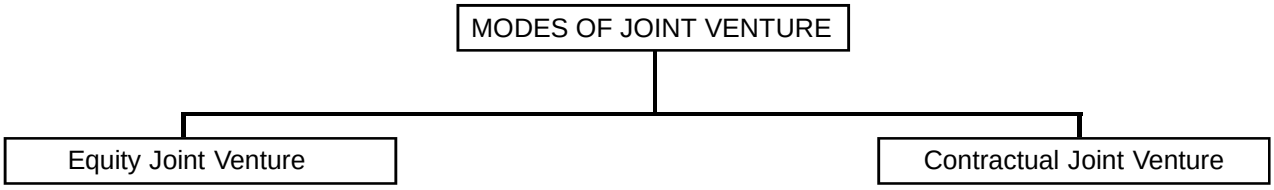
Because the amount and type of help needed from a partner may change over time, some companies opt to begin their venture under a shared management that they can later convert to a dominant venture. However, once both parents have become accustomed to operating the venture, such transitions become difficult to make.

The high failure rate of shared management ventures suggests that dominant ventures outperform shared management ventures. Since shared management ventures are not consistently used for riskier business tasks, their high failure rate is a strong indication that they are more difficult to operate than dominant parent ventures. Parents of the venture may, and often do, disagree over strategic and organizational decisions. Differences in the parent venture's priorities, direction, and perhaps values result in confusion, frustration, and slowness in the decision-making process and may place a joint venture at a distinct competitive disadvantage. As a result, if a partner is chosen for reasons other than managerial input a dominant parent structure will usually be best.

Majority ownership and dominance of a joint venture do not always go hand in hand. A parent holding only 24%

of one venture's shares may be its exclusive manager. Similarly, one parent may dominate a venture, despite the fact that it is a 50-50 deal.

MODES OF JOINT VENTURE



Equity Joint Venture

The equity joint venture is an arrangement whereby a separate legal entity is created in accordance with the agreement of two or more parties. The parties undertake to provide money or other resources as their contribution to the assets or other capital of that legal entity. The entity is generally established as a limited liability company and is distinct from either of the parties which participate in its creation. The newly created company, thus, becomes the owner of the resources contributed by the parties to the joint venture arrangement. Each of the parties in turn becomes the owner of the company having equity in the company.

The parties to a joint venture agreement agree on purposes and functions of the newly created entity, the proportion of capital contribution by each party and the share of each party in the profits of the company and on other matters such as its management, operation, duration and termination.

Contractual Joint Venture

The contractual joint venture might be used where the establishment of a separate legal entity is not needed or the creation of such a separate legal entity is not feasible in view of one or the other reasons. The contractual joint venture agreement can be entered into in situations where the project involves a narrow task or a limited activity or is for a limited term or where the laws of the host country do not permit the ownership of property by foreign citizens. For the purposes of contractual joint venture, the relationship between parties is set forth in the contract or agreement concluded between them.

Whether one or more of the legal methods are used in the establishment of the joint venture company to carry out its operations is always based on the negotiations between the parties, the results of which reflect in the joint venture agreement entered into between the parties. The licensing agreement, know-how agreement, technical services or technical assistance agreement, franchise agreement and agreement covering all other commercial matters might even form annexes to the main joint venture agreement. They can be signed once the joint venture company is established.

It is important to note that a joint venture agreement, be it for the establishment of a limited liability company or not, and the different contracts must be concluded in accordance with laws and regulations applicable to such companies including tax laws concerning these companies or the laws relating to agency or partnership as well as other economic laws, in addition to laws relating to labor, sales of goods, insurance and foreign economic and trade contracts.

A comparative study of Contractual Joint venture, Equity Joint Venture and Wholly owned subsidiary is given below:

	Contractual Joint Venture	**Equity Joint Venture**	**Wholly-Owned Subsidiary**
Structure	– Contract between the parties	– Separate legal entity, jointly owned by foreign party and local party	– Separate legal entity, 100% owned by foreign investor
Entry into Market	– Faster – Foreign party benefits from local party's customers, connections, knowledge of competitors, local laws and practices	– Faster – Foreign party benefits from local party's customers, connections, knowledge of competitors, local laws and practices	– Slower – Foreign investor has to grow business from scratch (e.g., hire employees, build demand, obtain sales)
Start-up costs	– Lower	– Lower to moderate – Costs of establishing and maintaining joint venture vehicle can be shared	– Higher – Costs of establishing and maintaining corporate entity borne solely by foreign investor
Resource Commitment	– Lower – Foreign party may, *e.g.,* license intellectual property or supply goods – Licensee/purchaser pays royalties/cash	– Lower to moderate – Foreign party often contributes management expertise, intellectual property and know-how – Local party often contributes employees, customers, plant and facilities	– Higher – Foreign investor must hire local employees and/or transfer expatriates, purchase raw goods, etc.
Intellectual Property Risk	– Higher – Potentially sharing or giving away IP to other party (i.e., a competitor;	– Higher – Potentially sharing or giving away IP to local party (i.e., a competitor)	– Lower – IP less exposed to a competitor because subsidiary is wholly-owned
Return on Investment	– Lower – Royalties generally yield lower returns than equity	– Moderate to higher – Equity generally yields higher returns than royalties, but returns are shared with other joint venture party – Foreign party may have licensed intellectual property to the joint venture vehicle in exchange for royalty payments	– Higher – Equity generally yields higher returns than royalties
Market Presence	– Lower – Foreign party not present in local market except through local party	– Moderate to higher – Foreign party has direct access to local market through local party	– Higher – Foreign investor has direct presence in local market
Political Risk	– Lower – Foreign party (licensor) does not bear risk of entry into volatile market	– Moderate – Foreign party bears partial risk of politically volatile market, government interference, nationalization	– Higher – Foreign investor bears full risk of politically volatile market, government interference, nationalization
Competition Law Risk	– Moderate to higher – Collaboration of competitors may trigger competition law obligations	– Moderate to higher – Participation by competitors in joint venture vehicle may trigger competition law issues	– Lower/none – No formal collaboration with a competitor, therefore generally no competition law concern
Control over Strategy	– Lower – Minimal integration of foreign party and local party's global strategy	– Moderate – Certain degree of control overjoint venture vehicle's global strategy – Dependent upon strategic objectives	– Higher – Complete control over wholly-owned subsidiary's global strategy

		of local party and ability of both parties to adhere to agreed strategy for the duration of the joint venture	
Complexity of Corporate Governance corporate control	– Lower – No joint corporate control	– Higher – Conflicting strategic visions, different management/cultural styles, unequal capital investments, and other material differences often require complex corporate governance mechanisms	– Lower – Foreign investor can exercise full control over wholly-owned subsidiary
Market Feedback	– Lower – No stand-alone entity for customers to identify with	– Moderate to higher – Joint venture vehicle may provide a direct identity and presence in the market	– Moderate to higher – Wholly-owned subsidiary provides direct identity and presence in the market
Formality	– Moderate – Need appropriate contracts – No need to form an entity	– Higher – Need a joint venture agreement and must form joint venture entity – Possible ancillary agreements (e.g., intellectual property license, management services, shareholder rights agreement)	– Moderate – Need to establish wholly-owned subsidiary
Complexity of Documentation	– Moderate to higher – Negotiation of license may be complex	– Higher – Negotiation of profit-sharing.	– Lower – No counterparty or joint venture partner
Termination Risk	– Moderate to higher – May be difficult to obtain market intelligence and transfer jointly- developed products out of joint venture (i.e., cost and ownership issues)	– Moderate to higher – May be difficult to obtain market intelligence and transfer jointly-developed products out of joint venture (i.e., cost and ownership issues) Potential for conflict over intellectual property developed during course of joint venture – Buy-out or termination procedures can be expensive and time-consuming	– Lower – Foreign investor owns 100% of subsidiary and, therefore, all of its assets

ADVANTAGES OF JOINT VENTURE

– International joint ventures allow for much faster and less costly access to foreign markets than can be achieved by purchasing an existing company in the jurisdiction or starting a new venture.

– IJVs provide quick access to channels of distribution, and they provide access for the non-resident partner to knowledge and know-how of the local marketplace, which substantially enhances the probability of success for the venture.

– The resident partner also often has existing relationships with key suppliers and customers, and proficiency in the local language and customs. These benefits can be especially critical to a small or medium-sized business that does not have the capital, resources or expertise necessary to pursue the opportunity unless it is able to share the risks and the costs through an alliance such as an international joint venture.

– IJVs allow the partners to move quickly, cost effectively and with credibility (provided by the reputation of the resident partner) in the local marketplace.

– The parties to an IJV can also take advantage of complementary lines of business and synergies that may exist between the two companies.

DISADVANTAGES OF JOINT VENTURE

- An international joint venture can result in a frustrating experience and ultimately a failure if it lacks adequate planning and strategy.
- Factors such as marketplace developments, technology issues, regulatory uncertainties and economic downturns can be difficult to anticipate and can have worse impact on IJVs.
- By their nature (and like all partnerships), profits derived from an IJV are diluted because they are shared.
- Management issues can arise, in spite of having adequate mechanisms in place to resolve disputes, because of different management philosophies of the partners.
- The partners also may discover that they do not share expectations and are not flexible enough to change and accommodate the evolving needs of the business.
- Joint ventures are often difficult to capitalize as an entity, particularly in respect to debt, because they are finite in their duration and therefore lack permanence.
- Unless an IJV is adequately capitalized, its debt financing, if available at all, may have to be guaranteed, in whole or in part, by the joint venture partners, which can increase their level of risk in the venture.
- Another potential disadvantage of an IJV is the possibility of the creation of a competitor or a potential competitor in the form of one's own joint venture partner.

TERMINATION OF JOINT VENTURES

Any number of events may lead to the termination of a JV. Many termination events are anticipated and provided for in the joint venture agreement. For example, a breach of the joint venture agreement may trigger termination or failure to meet research and development deadlines may lead to termination. A JV may terminate upon achieving its objectives. Alternatively, a JV may terminate upon failing to meet its objectives. The agreement could provide that one JVP buy the other out or sell its shares, or vice versa.

Excessive costs, failure to achieve projected income, or unforeseen capital requirements may make the continuation of a JV unattractive. In addition, a change in the JV's objectives or those of a shareholder may also lead to the early termination of the JV. Changes in objectives may result from a JVP's internal strategic redirection, competitive advances, or market changes beyond the control of the JV or its shareholders. Disagreement by JVPs on fundamental management issues may also lead to termination.

An obvious disadvantage of sharing capital obligations is the need to share profits generated from the actual operation of the JV. Issues can arise in this area because of the fact that parties will also be contributing intangible assets to the business, such as intellectual property rights and technical expertise. Technology and management sharing can potentially create significant problems among the parties. In particular, one party's mastery of the other's technology can lead to improvements on that technology beyond the intended services of the JV, a factor that tends to discourage companies from disclosing their technologies for fear of losing the competitive edge to their JVP.

However, JVs offer a structure where both partners contribute to the costs associated with the exploitation of the technology in proportion to their expected benefits. The motive of forming a joint venture is to gain from the venture by both the parties and terminate the venture when the desired objective is fulfilled.

Examples of Joint Ventures

Party to Joint Venture	Percent Participation	Value in US Dollar	Brief of the Venture
IBM (U.S.) and Lenovo Group(China) (2004)	18.9/81.1	$1.75 billion	IBM sold its PC division to China-based Lenovo Group. Companies entered into a joint venture that would make Lenovo the third largest PC maker in the world, behind Dell and Hewlett Packard, and give IBM an 18.9 percent stake in Lenovo.
Skype Software (Denmark) and Tom Online (China) (2005)	49:51	$1.75 billion	Skype formed a joint venture with Tom Online, China's leading wireless Internet provider. Joint venture developed, customized and distributed a simplified Chinese version of the Skype's Voice over Internet Protocol software and premium services to Internet users and service providers in China.
Areva SA (France) and Energy Constellation (U.S.) (2005)	50:50	$11 billion	Areva SA, a multinational industrial conglomerate that deals in energy, and Constellation Energy, that generated trades, supplied and distributed energy, formed a joint venture, UniStar Nuclear, to sell next-generation nuclear plants in the U.S. Areva will be the prime contractor for the new plants, providing the first load of nuclear fuel, while Constellation will run the plants and hold their operating licenses.
Pontiac Land Group (Singapore) and West Paces Hotel Group (U.S.) (2006)	50:50		Pontiac and West Paces formed a joint venture known as the West Paces Hotel Group Asia. Headquartered in Singapore, this hotel management company will introduce new luxury hotels across Asia. Pontiac Land will focus on business development and securing strategic partnerships in Asia with leading high net-worth families and institutions. West Paces Hotel Group, headquartered in Atlanta, Georgia (USA), will contribute management and operations expertise in designing properties geared toward affluent travelers.
Siemens AG (Germany) and Nokia Corp.(Finland) (2006)	50:50	$19.9 billion	Siemens AG and Nokia Corp. combined their fixed and mobile network infrastructure businesses in a joint venture known as Nokia Siemens Networks. The JV formation was a reaction to recent mergers in the industry, such as Alcatel with Lucent, and the rise of low-cost Chinese competitors such as Huawei Technologies Co Ltd and ZTE Corp. Nokia Siemens Networks became the second largest company, behind Ericsson, in wireless networks and third in fixed-line, behind Alcatel and Cisco Systems and is headquartered in Finland.

Hit Company (Rep. of Slovenia) and Harrah's Entertainment (U.S.) (2007)	50:50	$700 million	Slovenian gaming company Hit and U.S. casino operator Harrah's Entertainment formed a JV to build a major new gaming and entertainment center in Slovenia, scheduled for completion in 2009 provided that the Slovenian government loosens gaming legislation. The project rests on the Slovenia government's willingness to tweak legislation: currently, foreigners can hold no more than 20% in a gaming venture, and the gaming tax is set at a high 30%. Harrah's was in talks with the government on changes to the gaming law that would allow foreigners to hold a 50% stake. Harrah's would also like the government to lower the gaming tax.
Posco (South Korea), SeAH Corp. (South Korea) and U.S. Steel (U.S.) (2007)	35:30:35	$93 million	U.S. Steel partnered with Posco, South Korea's leading steel producer, and SeAH, a tubular steel maker, in the venture to be called United Spiral Pipe LLC, to build a new U.S. facility that will produce spira- welded pipe for the natural gas industry.

JOINT VENTURE AGREEMENTS

The joint venture documents and agreements are critical to the success of the venture. The joint venture agreement forms the basis of the understanding between and among the parties. It is relied upon to ensure that all parties understand their roles, rights, responsibilities, and remedies in the conduct of the venture. Organizations enter into joint ventures in good faith but closely scrutinize the joint venture documents if anything goes awry.

The importance of the documents and the purpose of this part are to cover, step by step, the critical elements to consider and include in joint venture agreements. Equity participation, for example, may or may not be as important as operational control. Technical participation in the venture may or may not be as important as the intellectual property rights that may result from the venture. A key to developing joint venture agreements is to determine goals and objectives in advance and ensure that the interests are reflected in the agreement.

Selection of a good local partner is the key to the success of any joint venture. Personal interviews with a prospective joint venture partner should be supplemented with proper due diligence. Once a partner is selected generally the parties highlighting the basis of the future joint venture agreement sign a memorandum of understanding or a letter of intent. Before signing the joint venture agreement, the terms should be thoroughly discussed to avoid any misunderstanding at a later stage. Negotiations require an understanding of the cultural and legal background of the parties.

In the definitive IJV agreement, the following principal matters should be dealt with comprehensively:

1. **Purpose of Joint Venture:** A well defined objective is one of the most important and crucial issues in the joint venture agreement. The parties should arrive at some understanding to identify and define in clear terms the basic purposes of the proposed joint venture. Therefore in identifying and defining the basic objectives of the proposed joint venture company, the parties must take into account the scope and size of joint venture business, management and operational responsibilities of parties, decision making process, terms of any ancillary agreement between joint venture and either of the parties etc.

2. **Contributions by Parties:** The agreement should describe in as much detail as possible the respective contributions of the parties, both tangible and intangible. Depending on tax considerations, it may be appropriate to specify values for the respective contributions of the parties. While planning and negotiating the proportion of contributions to be made by the parties in the proposed enterprise, the issues relating to financial, technical and functional requirements of the joint venture throughout the proposed term of its existence must be discussed and analyzed threadbare. Since the parties are something more than passive investors in the joint venture, the range of possible contributions are much broader than is normally required. For instance the parties will contribute cash and cash equivalents to finance the operations of the joint venture, they may also provide the venture with services, tangible and intangible property rights and specific functional expertise in areas such as research and development, manufacturing and distribution. In addition, parties may contribute their experience and contacts in dealing with local regulators and in obtaining supplies of scarce raw material.

3. **Capital Structure:** The capital structure is an essential element of a business venture. Therefore, the issues relating to capital structure should be clearly defined in the joint venture agreement, so as to avoid any dispute between the parties concerning return on invested capital, management, control and administration of the enterprise. As the parties become the owner of the enterprise on its formation, they acquire such rights as may be created under the laws of the host country as well as any contractual agreement between the parties.

4. **Management, Control and Administration:** Devising an appropriate governance structure for a joint venture company is of critical importance to the success, growth and development of that company**.** It is critical that senior management be chosen early, be independent, have a clear charter and authority, and have clear reporting lines. It is in this connection very common for companies to enter into contract with one or more of the parties to conduct some specific functions and services including even basic research and development, manufacturing and distribution, thus as a consequence to these agreements, the party(ies) effectively assume control over operations of the enterprise, even though the nominal authority rests with the board of directors and managers of the companies. Therefore, to avert such happenings in the management and administration of joint venture, the parties must strike a balance between the powers and right of parties and the board of directors. As the joint venture companies are an independent legal entity with life of its own, it is of great importance to the parties to include in joint venture agreement key issues relating to operation of enterprise, such as legal compliances, insurance, disclosure of information, accounting and financial reporting including allocation and distribution of joint venture income.

5. **Governance:** The structure of the board of directors of the joint venture entity (or the committee that will provide management oversight in the case of a contract joint venture or a non corporate entity) should be given careful thought and specified with particularity. The board should be comprised of an odd number of directors. It is common for the two joint venture partners' representatives to agree upon the odd numbered director.

6. **Allocation of Risks and Rewards:** In as much detail as possible, the parties should delineate who gets what, where, when, why and how. Dividend distributions, capital calls and allocations of losses (including special tax allocations, if permissible) should be covered.

7. **Alternative Dispute Resolution Provisions and Deadlock Provisions:** Most joint venture partners will not choose to risk litigation in either of their respective forums. Detailed provisions and procedures for mediation and/or arbitration should be set forth. In addition, consideration should be given to impasse provisions short of mediation or arbitration as a way to resolve deadlocks that are not fatal to the joint venture.

8. **Continuity of Joint Venture Termination Provisions** - Detailed provisions should be inserted regarding when and how the agreement and joint venture terminate. If either party is to have an opportunity to buy the interest of the other party, that mechanism should be both well thought out and set forth in detail. The Joint Venture Agreement is an agreement in perpetuity. It lasts so long as the parties to the Joint Venture continue to be in business. However, situations may arise when one of the parties want to pull out of joint venture arrangement. In such cases, the outgoing party will have to make a first option of purchase of its interest to the other party to the Joint Venture. If this fails, the outgoing partner will have the option of bringing a new party to the Joint Venture in which case all the provisions of the Joint Venture agreement will apply to the new party, as if the new party had been a signatory to the Joint Venture agreement.
9. **Issue of Further Capital:** Another crucial issue in a Joint Venture is the issue of further capital by the Joint Venture Company. In order to maintain the proportion of capital contributed by the parties to the Joint Venture, further issue of capital is strictly regulated, subject to unanimous consent of the entire Board of directors and not by majority decision.
10. **Operational Issues:** Besides issue of further capital, a number of other operational issues like borrowing of capital, expansion and diversification of business of joint venture dividend policy, investment by the joint venture in the purchase of shares of other companies etc. are crucial in respect of which the articles of association of the joint venture company provides for unanimous consent of the Board, in which the joint venture parties are represented ,proportionate to their voting strength.
11. **Regulatory Issues:** All regulatory issues affecting the joint venture should be dealt with and, set forth clearly. Those issues include, export and import controls, foreign corrupt practices act (and its equivalent) compliance, companies acts (and their equivalent) and competition law (anti-trust) compliance. In a few jurisdictions, currency repatriation must also be addressed.
12. **Ownership Transfer –** In an equity IJV, provisions should set forth the restrictions on the transferability of ownership interests in the joint venture entity. The parties may agree to a variety of possible transfer arrangements, including rights of first offer, rights of first refusal etc.
13. **Governing Language -** IJV agreements are often written in languages of both the concerned parties. However, one language should be designated to prevail if there is an alleged inconsistency between the documents and their translations.
14. **Restrictive covenants:** A Restrictive Covenant is a specific type of covenant in which someone agrees to be restricted by a contract. The most common type of restrictive covenant is one in which a former employee is restricted from working in his or her field for a specific time and within a specific area after leaving employment. It the venture parties enter into restrictive covenants or have a memorandum of understanding in the complex area of parallel or related businesses must be discussed. Whether an IJV is dissolved or ends by one party purchasing the interest of another, non-competition provisions may well be appropriate. In addition, parties commonly seek non-disparagement, confidentiality and non-solicitation of employee covenants.
15. **Intellectual Property Provisions** - The IJV agreement or a separate attached document should clearly delineate all rights to IP, technology, software and the like. In addition, an appropriate licensing agreement should be executed in respect to those “knowledge” items. The IJV agreement should clearly delineate ownership of intellectual property upon dissolution or termination of the joint venture.

A detailed List of basic clauses in a Joint Venture Agreement is given below:

(1) Identification of parties

(2) Objectives of the joint venture

(3) Assignability

(4) Consents and approvals

(5) Compliance with laws

(6) Nature of company to be formed

(7) Capital of company

(8) Ordinary course of business

(9) Access to and preservation of business records

(10) Title to assets

(11) Percentage ownership of each party

(12) Outstanding capital stock

(13) Transfer of shares

(14) Transferee's adherence agreement

(15) No violation

(16) Share structure

(17) Voting rights

(18) Quorum rights

(19) Dividend policy

(20) Qualified majority on key issues

(21) Board of directors

(22) Management

(23) Financial statements

(24) Accounting

(25) Due diligence procedures

(26) Environmental issues

(27) Employee related facts

(28) Taxes

(29) Commissions

(30) Disclosure

(31) Material adverse change

(32) Representations or warranties

(33) Indemnification

(34) Opinion letter

(35) Non-competition

(36) Equal opportunity;

(37) Survival of joint venture agreement and buyer's/seller's knowledge of defects;

(38) Confidentiality;

(39) Settlement of dispute mechanisms;

(40) Time limitations;

(41) Amendments;

(42) Merger or entire agreement clause;

(43) Waivers;

(44) Arbitration or court;

(45) Applicable law;

(46) Brokers and finders;

(47) Expenses and costs;

(48) Force majeure;

(49) Nationalization and privatization

(50) Notices

DRAFTING OF A JOINT VENTURE OR FOREIGN COLLABORATION AGREEMENT

It is difficult to prepare a set frame of the terms and conditions. The conditions may differ according to the requirements. While drafting a foreign collaboration agreement, the following factors should be kept in mind:

- *Capability of the collaborator and the requirements of the party are clearly indicated.*
- *Clear definitions of technical terms are given.*
- *Specify if the product shall be manufactured/ sold on exclusive or non-exclusive basis.*
- *Terms and conditions regarding nature of technical know-how, disclosure of drawings, specifications and other documents, furnishing of technical information in respect of processes with flow charts etc., plant outlay list of equipment, machinery and tool with specification have to be provided.*
- *Provisions for making available the engineers and/or skilled workers of the collaborator on payment of expenses relating to their stay per diem etc. are given.*
- *Details regarding specification and quality of the product to be manufactured are given.*
- *Quality control and trademarks to be used are also specified.*
- *Responsibility of the collaborator in establishing or maintaining assembly plants should be clearly determined and provided for.*
- *If sub-contracting of the work is involved, clarify if there would be any restrictions.*
- *The rate of royalty, mode of calculation and payment etc. Also, make provision as to who will bear the taxes/cess on such payments.*
- *Use of information and industrial property rights should also be provided for in the agreement.*
- *A clause on force majeure should be included.*
- *A clause that the collaborating company has to train the personnel of Indian company within a specified*

period should be incorporated The clause should also specify the terms and conditions of such assistance, place of training, period of training and fees payable.

– *A comprehensive clause on arbitration containing a clear provision as to the kind of arbitrator and place of arbitration should be included.*

– *There should be provision in the agreement for payment of interest on delayed payments.*

SELF STUDY

– Fuji Xerox is one of the most enduring and successful joint ventures. You are to find out factors which led to the success of this joint venture.

– Identify some other joint ventures which have been highly successful and some ventures which have failed badly. Do a comparative study of the reasons for success and failure of the ventures.

SPECIMEN JOINT VENTURE AGREEMENT

THIS AGREEMENT made today of ……BETWEEN……. – a company registered in India under the Companies Act 1956 having its registered office at……. (hereinafter referred to as the Indian Company) which expression shall, unless repugnant to the context or meaning thereof, is deemed to include its successors and assigns of the ONE PART AND…….. – A German corporation, with place of registry in and having an office at…… (hereinafter referred to as the Foreign Company) which expression shall, unless repugnant to the context or meaning thereof, be deemed to include its successors and assigns of the OTHER PART.

WHEREAS –

1. The Indian Company intends to establish a self-sufficient and well-equipped industrial unit in India for the purpose of developing, manufacturing and marketing of the products, fully described and specified in the Schedule-A hitherto (hereinafter referred to as the said products).
2. The Indian company has obtained necessary License from the Government of India for an initial production capacity of 1 per year subject to the terms and conditions specified in the said License.
3. The Foreign Company has for many years in past been carrying on manufacture, marketing, sale and distribution of the said product in and has acquired considerably technical skill and expertise in the field of this business.
4. The Foreign Company, by virtue of its specialization in the field of this business, is in possession of extensive technical know-how concerning the setting up of a modern manufacturing unit for the manufacture of the said products in India or elsewhere and has at its disposal sufficient skilled technical personnel to provide technical assistance in the nature of consultancy, advisory and operating services to the Indian Company.
5. The Indian Company is desirous of acquiring from the Foreign Company the said specialized services in the nature of consultancy, advisory and operating services in the matter of settling up of a new manufacturing unit for the Indian Company in India.
6. The Foreign Company has agreed to provide the said technical assistance by way of consultancy, advisory and operating services for setting up of a new self-sufficient unit for the purpose of manufacturing, marketing, sale and distribution of the said products in India by the Indian Company upon the terms, conditions and stipulations set forth herein.

NOW THIS AGREEMENT WITNESSETH and it is hereby agreed by and between the parties as follows:

1. Technical Services

The Foreign Company shall render the following technical services to the Indian Company:

(i) Feasibility study for the proposed project, including market survey, profitability, cash flow projections and preparation of comprehensive project report.

(ii) Provide manufacturing/engineering technology available with the Foreign Company relating to design, production method, and manufacture and testing of the said products, to the Indian Company.

(iii) Explore for adaptation of the requisite local technology, expertise and skill.

(iv) Assist in the manufacture and development of the said products according to the required standard and technology.

(v) Assist in regular research and quality control of the raw materials and the finished products and to explore suitable substitutes acceptable to customers.

(vi) Advise proper marketing, selling and distribution techniques appropriate for the said products.

(vii) Assist and advice in the procurement of appropriate raw materials and explore and advice suitable import substitutes.

(viii) Advise production-planning appropriate for optimum utilization of the rated production-capacity maintaining plant and machinery for the manufacture of the said products to the required standard.

(ix) Assist and advice in setting up ancillary small and medium scale industries for the growth and development of the Indian Company's factory.

(x) Advise introduction of operation and maintenance system suitable for the plants and machineries to be used in the manufacturing process to ensure safe and efficient normal life.

(xi) To assist and advice appropriate safety measures and appropriate appliances to comply with the statutory requirements and otherwise.

(xii) To assist in the preparation of a list of – maintenance spares required for various plants and machineries to be used in the factory.

(xiii) To assist in the cost and budgetary control.

(xiv) To assist in conducting constant market research and advice change in the product-design or sales engineering according to the changed demand of the customers.

2. Deputation of technical personnel

(i) It is understood and agreed that the Foreign Company shall provide technical services hereunder by and through its own technical personnel or by and through any of the Foreign Company's associate company acceptable to the Indian Company.

(ii) The Foreign Company shall depute from its trained technical personnel such number of staff not exceeding ……employees as and when required by the Indian Company to assist the Indian Company in setting up of the proposed manufacturing unit and its running and maintenance.

(iii) Besides the technical services enumerated in clause 1 hereof, the technical personnel deputed by the Foreign Company shall also be responsible for rendering the following services:

(a) Making periodical site inspection of and during the construction of the factory at the cost and expenses of the Indian Company, as may be necessary and also to cause periodical checking whether the factory is being constructed by the Indian Company in compliance with the instructions, specifications and standards supplied by Foreign Company.

(b) Assisting in the procurement of the required plant, machinery and equipment for the proposed factory from appropriate sources and inspecting the same at the supplies premises before they are supplied to ensure their correctness and standard.

(c) Holding conference with engineers, contractors, specialists and architects from time to time to advise the Indian Company upon the techno-commercial supervision of the factory in order to ensure maintenance of the factory according to the standard and technical specifications laid down by the Foreign Company.

(iv) The technical personnel so deputed by the Foreign Company shall remain employees of the Foreign Company but while working in the factory of the Indian company they shall be subject to all the rules and regulations of the Indian Company as applicable to their employees.

3. Training of personnel of the Indian Company

(i) During the term of this agreement the Foreign Company shall undertake from time to time to train personnel of the Indian Company for training in its plant in ……..

(ii) The training shall be for such period and for such number of personnel as may from time to time be mutually agreed upon by the parties.

(iii) The Foreign Company ensures that the training of the personnel of the Indian Company as may be imparted shall be adequate to impart complete competency in the respective fields for independent performance of the required functions for the Indian Company.

(iv) The Indian Company shall obtain prior approval of the Government, wherever necessary, for the purpose of deputation of their personnel for the training abroad to the Foreign Company.

(v) The Indian Company shall be responsible for and bear all expenses incidental to such training of their personnel, provided that no additional charges shall be payable by the Indian Company to the Foreign Company for importing such training to the personnel of the Indian Company.

(vi) The personnel of the Indian Company shall during the period of their training observe all the rules and regulations as applicable to the employees of the Foreign Company.

4. Secrecy

(i) It is hereby agreed and declared that all written advises and materials and all drawings, documents, specifications and technical know-how under this agreement in pursuance of the technical services to be rendered by the Foreign Company to the Indian Company shall be held in strict confidence and secrecy and shall not be disclosed by the Indian Company or any of its employee without written prior permission of the Foreign Company during the term of this agreement to any third party.

(ii) In the event of termination of this agreement on account of any default whatsoever by the Indian Company, all such documents and materials shall be returned by the Indian Company to the Foreign Company.

5. Consideration

In consideration of the Technical Services to be rendered by the Foreign Company to the Indian Company under this agreement, the Indian Company shall pay the following Technical Services fee to the Foreign Company:

(i) For the first 3 years from the date of commercial production a sum of ' ……. (Rupees…….) only per annum is payable half yearly within seven days from the last day of the preceding month.

(ii) For the next 2 years thereafter, a sum of Rs……..(Rupees……..only) per annum is payable in the above manner.

(iii) All such payments shall be payable by the Indian Company to the Foreign Company in the …….currency, subject to Indian taxes, at the Registered Office of the Foreign Company through normal banking channels.

6. Prior Government approval

This agreement shall be subject to the prior approval being obtained by the Indian Company and the Foreign Company from the appropriate authorities in their respective countries in respect of the transaction herein contemplated, such approval being obtained within 12 months from the date hereof and in the event such approval not being obtained with the said period of 12 months by either party, the other shall have the right to rescind this agreement. In the event such approval is obtained within the said period the effective date of this agreement shall be construed as the date on which this agreement has been taken on record by the Government for the purpose of such approval.

7. Duration of the agreement

(i) This agreement shall come into force on and from the "effective date" defined in clause 6 hereinabove and shall remain in force for a period of five years therefrom or five years from the date of the commencement of regular commercial production of the said products, whichever is later, provided such production is not delayed beyond three years from the "effective date" of this agreement.

(ii) Subject to the approval of the appropriate Government authorities, this agreement may be renewed in whole or in part for a further period by mutual agreement, provided negotiations for extension shall be taken up one year prior to the expiry of the term of this agreement.

(iii) This agreement shall be binding upon and inure to the benefit of the successors and assigns of the respective parties hereto, and the obligations hereunder shall not be assignable by the either party without the consent in writing being first obtained from the other.

8. Termination of the agreement

Notwithstanding anything contained herein, either party may by notice in writing to the other party terminate this agreement under any one of the following conditions

(i) If the Foreign Company fails to perform or observe any of its obligations under this agreement which it is obliged to perform or observe hereunder.

(ii) If either party discontinue business or be adjudicated insolvent or bankrupt or make an assignment for the benefit of creditors or a composition with creditors or shall file a voluntary petition of winding up or shall answer admitting the material allegations of an involuntary petition pursuant to any applicable law of any jurisdiction or if any order is entered appointing a receiver or trustee of either party or of a substantial portion of assets of either party or if either party applied for a consent to the appointment of such receiver or trustee.

(iii) If there is a change in the existing management and/or constitution of the business of the Indian Company whether through the alienation of shares, or through the increase of capital and the issue of new shares, or otherwise howsoever, unless the matters and effects arising out of such change are remedied and mutually settled by a written instrument by the parties hereto within 90 days from the date when such change first occurs.

(iv) If at any time during the term of this agreement either of the parties hereto fails to perform its respective obligations hereunder, the other party shall have the right to terminate this agreement by giving 90 days' notice in writing setting forth the breach of obligation under this agreement complained of and unless the breach is cured within 30 days from the date of such notice, the agreement shall be terminated on the expiry of 90 days and the rights of the parties hereunder shall cease upon the date so specified in the notice.

(v) Upon the termination of this agreement for any reason whatsoever, all amount due and owing as between the parties shall become due and be paid within 30 days from the date of termination of this agreement.

9. Force Majeure

No party to this agreement shall be responsible for any failure or delay on its part in performing any of its obligations or for any loss, damages, costs, charges or expenses incurred or suffered by the other party by reason of such failure or delay if such failure or delay is caused due to any force majeure conditions, such as acts of God, Government laws and regulations, strikes, Lockouts, war or any other causes beyond its control.

10. Arbitration

In case of any dispute or difference arising between the parties hereto or any claim or thing herein contained or the construction thereof or as to any matter in any way connected with or arising out of these presents or the operation thereof the rights, duties or liabilities of either party thereof, then and in every such case the matter, differences and dispute shall be referred to an arbitrator in India in case parties agree upon one, otherwise two arbitrators in India, one being nominated by each party to this agreement in accordance with and subject to the provisions of the Arbitration and Conciliation Act, 1996, or any other enactment or statutory modifications thereof for the time being in force.

11. Miscellaneous

(i) This agreement, either whole or in part, or any rights given hereunder cannot be assigned or transferred in any manner whatsoever by either party without the prior written consent of the other party.

(ii) This agreement cannot be altered or modified otherwise than by a written instrument duly signed by both the parties.

(iii) Any notice required to be given under this agreement shall be in writing and sent by post addressed to either of the parties at their Registered addresses.

12. Law applicable

This agreement shall be construed in accordance with and be governed by the laws of India.

IN WITNESS WHEREOF the parties hereto have hereunto caused their respective Common Seal to be hereunto affixed the day, month and the year first above written.

Signed Sealed and Delivered by (FIRST PARTY) the Common Seal of …….. Company was hereunto affixed pursuant to a resolution of its Board of Directors passed in that behalf on …….in the presence of Mr.…… its Secretary who have signed in the presence of Signed Sealed and Delivered by (SECOND PARTY) the Common Seal etc.

INTERNATIONAL COMMERCIAL ARBITRATION

Introduction

Whenever two or more parties have a dispute, it would be preferable if they were able to discuss it between themselves and to arrive at a peaceful solution. That is true whether the parties are members of a family, States or commercial entities. Only the parties themselves can achieve a solution that will not only resolve the dispute, but will facilitate a useful future relationship. However, sometimes the parties are not interested in any future relationship and only want the dispute to be settled, preferably on their own terms. That may lead to war or its private equivalents. Even when they are interested in a peaceful settlement of the dispute, it is not infrequent that the parties are not able to discuss – or negotiate – a mutually agreeable solution. In such a situation the aid

of a third party must be sought. The State offers one form of third party settlement of private disputes by maintaining a court system in which they can be litigated. Most private disputes that require the services of a third party are settled by litigation, though many of them are settled directly between the parties once the litigation has begun. It is also possible for the parties to involve third persons in a private capacity to solve, or to help them solve, the dispute. Arbitration is the more prominent of the private dispute settlement mechanisms, both domestically and for international commercial relations. "International Commercial Arbitration" is a particular means of settling disputes, i.e. by "arbitration" that is "commercial" in nature and has some international element to it. The term has been explained in detail in following paragraphs.

International

In the UNCITRAL Model Law on International Commercial Arbitration, arbitration is international if any one of four different situations is present:

(1) The parties to the arbitration agreement have, at the time of the conclusion of the agreement, their places of business in different States. This rule is then modified to provide that "If a party has more than one place of business, the place of business for determining whether the arbitration is international is that which has the closest relationship to the arbitration agreement." Therefore, under this provision, if the local office in State A of a multinational company from State B enters into a contract with a company from State A calling for arbitration in State A, the arbitration would not be international in State A.

(2) The place of arbitration, if determined in or pursuant to, the arbitration agreement, is situated outside the State in which the parties have their places of business. Under this provision two parties from State A might agree to arbitrate in State B. If State B had adopted the Model Law, the arbitration would be international in State B.

(3) Any place where a substantial part of the obligations of the commercial relationship is to be performed or the place with which the subject-matter of the dispute is most closely connected is situated outside the State in which the parties have their places of business. Under this provision arbitration in State A between two parties from State A in regard to a construction project situated in State B would be an international arbitration.

(4) The parties have expressly agreed that the subject-matter of the arbitration agreement relates to more than one country.

Commercial

The term 'commercial' should be given a wide interpretation so as to cover matters arising from all relationships of a commercial nature, whether contractual or not. Relationships of a commercial nature include, but are not limited to, the following transactions: any trade transaction for the supply or exchange of goods or services; distribution agreement; commercial representation or agency; factoring; leasing; construction of works; consulting; engineering; licensing; investment; financing; banking; insurance; exploitation agreement or concession; joint venture and other forms of industrial or business co-operation; carriage of goods or passengers by air, sea, rail or road.

Arbitration

It is not defined in the UNCITRAL Model Law on International Commercial Arbitration. However it has following principal characteristics.

1. **Arbitration is a mechanism for the settlement of disputes:** If there is no dispute, there can be no arbitration. The issue arises most often when one party fails to pay a sum of money owed to the other, perhaps in the form of a negotiable instrument, and the debtor does not dispute the obligation. If there

is an existing arbitration clause, the creditor can or must invoke the arbitration clause or, there being no dispute as to the existence of the obligation, the creditor can seek enforcement of the obligation by court action. The question of settlement might also arise if it appears that the parties agreed to arbitration in order to secure an enforceable award

2. **Arbitration is consensual:** arbitration must be founded on the agreement of the parties. Not only does this mean that they must have consented to arbitrate the dispute that has arisen between them, it also means that the authority of the arbitral tribunal is limited to that which the parties have agreed. Consequently, the award rendered by the tribunal must settle the dispute that was submitted to it and must not pronounce on any issues or other disputes that may have arisen between the parties.

3. **Arbitration is a private procedure:** Arbitration is not part of the State system of courts. It is a consensual procedure based on the agreement of the parties. Nevertheless, it fulfils the same function as litigation in the State court system. The end result is an award that is enforceable by the courts, usually following the same or similar procedure as the enforcement of a court judgment. Consequently, the State has an interest in the conduct of arbitration beyond the interest it has in the settlement of disputes by other procedures that are also alternatives to litigation.

4. **Arbitration leads to a final and binding determination of the rights and obligations of the parties:** Many arbitration rules, such as ICC Arbitration Rule 28(6), specifically provide that *"Every Award shall be binding on the parties. By submitting the dispute to arbitration under these Rules, the parties undertake to carry out any Award without delay".*

Benefits of international commercial arbitration

(1) **Avoids litigating in foreign court:** The most favorable situation for a party to a dispute in an international commercial transaction is to litigate in one's own courts. Even if the courts are scrupulously unbiased, that party is litigating at home using its regular lawyers, following a familiar procedure and in its own language. While that is good for one party to the transaction, it is not so good for the other party who faces all the difficulties of litigating in an unfamiliar procedure, in a language that may be foreign and may not be the language of the contract, and not being able to use its lawyers who are familiar with the company. It is also not irrelevant that the one party is staying at home while the other party is staying in a foreign country with all the inconvenience and expense that entails.

(2) **Arbitration reduces inequalities:** Arbitration of such disputes is a means to reduce the inequalities. While it is possible for the arbitration to take place in an arbitration organization located in the home country of one or the other party, it is also possible for the arbitration to be administered by an arbitration organization located in a third country. Furthermore, many arbitration organizations will administer arbitrations throughout the world. There is active competition among leading arbitration organizations to offer their services worldwide. An interesting example is provided by the American Arbitration Association. It has a long and distinguished history as a provider of domestic arbitration services. In order to reduce any image of partiality that might be conveyed by its name, it offers its services as a provider of arbitration services for international disputes through its International Center for Dispute Resolution, which has a European office in Dublin, Ireland.

(3) **Reduces chances of partiality of the courts w**hen State is party**:** There are special concerns about the partiality of the courts when the State is a party to the dispute. The State has too many means to influence decisions in its own courts for foreigners to feel comfortable litigating against it there. The same might be said about arbitrating against the State in an arbitration organization located in that State. This factor is the major reason for the extraordinary increase in the number of bilateral investment treaties in recent years in which foreign investors have the option of instituting arbitration in one of several arbitration forums outside the host State.

(4) **Ease of enforcement:** A final reason for the current popularity of international commercial arbitration is the comparative ease of enforcement of an award as compared to the enforcement of a judgment of a foreign court. Unless there is a treaty between the State in which the judgment was issued and the State in which enforcement is sought, the requested court is under no international obligation to enforce the judgment. While there a number of bilateral treaties for the enforcement of judgments.

EXAMPLES OF SOME ARBITRATION CLAUSE IN JOINT VENTURE AGREEMENT

The drafting of an arbitration clause appears straightforward, but there are a number of matters which should be considered. Given below are the clauses recommended by the ICC, the LCIA and the ICA, together with an example of an *ad hoc* clause.

A. ICC Recommended Arbitration Clause

"All disputes arising in connection with the present contract shall be finally settled under the Rules of Conciliation and Arbitration of the International Chamber of Commerce by one or more arbitrators appointed in accordance with the said Rules.Parties are reminded that it may be desirable for them to stipulate in the arbitration clause itself the law governing the contract, the number of arbitrators and the place and language of the arbitration. The parties' free choice of the law governing the contract and of the place and language of the arbitration is not limited by the ICC Rules of Arbitration.Attention is called to the fact that the laws of certain countries require that parties to contracts expressly accept arbitration clauses, sometimes in a precise and particular manner".

B. ICA Recommended Arbitration Clause

"All disputes or differences whatsoever arising between the parties out of or relating to the construction, meaning and operation or effect of this contract or the breach thereof shall be settled by arbitration in accordance with the Rules of Arbitration of the Indian Council of Arbitration."

C. Example of Indian Collateral Agreement

"All disputes and differences arising out of or in relation to the contract dated…… entered into by the parties hereto, and all or any questions concerning the existence and/or validity of the said contract (or any of its terms) shall be referred to and settled by arbitration in accordance with the Rules of Arbitration of …."

D. LCIA Recommended Arbitration Clause

Parties to an international contract who wish to have any disputes referred to arbitration under the LCIA Rules are recommended to insert in the contract an arbitration clause in the following form:

"Any dispute arising out of or in connection with his contract, including any question regarding its existence, validity or termination, shall be referred to and finally resolved by arbitration under the Rules of the London Court of International Arbitration, which Rules are deemed to be incorporated by reference into this clause".

Parties are also reminded that difficulties and expenses may be avoided if they expressly specify the law governing their contract. The parties may if they wish also specify the number of arbitrators, and the place and language of the arbitration. The following provisions may be suitable:

"The governing law of this contract shall be the substantive law of……"

"The tribunal shall consist of ……. (a sole or three) arbitrator(s)."In the case of a three-member tribunal, the following words may be added"….two of them be nominated by the respective parties"

"The place of the arbitration shall be …..(city)"

"The language of the arbitration shall be ….."

E. Example of an ad hoc Arbitration Clause

"Any dispute, controversy or claim arising out of or in relation to this contract or its breach, termination or invalidity shall be settled by arbitration in accordance with the UNCITRAL Arbitration Rules, and the appointing authority shall at the time be the President of the Indian Chamber of Commerce".

UNCITRAL MODEL LAW ON INTERNATIONAL COMMERCIAL ARBITRATION

The United Nations Commission on International Trade Law (UNCITRAL) is a subsidiary body of the General Assembly. It plays an important role in improving the legal framework for international trade by preparing international legislative texts for use by States in modernizing the law of international trade and non-legislative texts for use by commercial parties in negotiating transactions.

UNCITRAL legislative texts address international sale of goods; international commercial dispute resolution, including both arbitration and conciliation; electronic commerce; insolvency, including cross-border insolvency; international transport of goods; international payments; procurement and infrastructure development; and security interests. Non-legislative texts include rules for conduct of arbitration and conciliation proceedings; notes on organizing and conducting arbitral proceedings; and legal guides on industrial construction contracts and countertrade.

The United Nations Commission on International Trade Law on 21 June 1985, adopted UNCITRAL Model Law on International Commercial Arbitration recognizing the value of arbitration as a method of settling disputes arising in international commercial relations, and convinced that the establishment of a model law on arbitration that is acceptable to States with different legal, social and economic systems will contribute to the development of harmonious international economic relations.

The Model Law, together with the Convention on the Recognition and Enforcement of Foreign Arbitral Awards and the Arbitration Rules of the United Nations Commission on International Trade Law recommended by the General Assembly significantly contributes to the establishment of a unified legal framework for the fair and efficient settlement of disputes arising in international commercial relations.

The important provisions of the Model Law as amended by UNCITRAL in 2006 are given hereunder:

Article 1: Scope of application

Arbitration is international if:

(a) the parties to an arbitration agreement have, at the time of the conclu-sion of that agreement, their places of business in different States; or

(b) one of the following places is situated outside the State in which the parties have their places of business:

– the place of arbitration if determined in, or pursuant to, the arbitration agreement;

– any place where a substantial part of the obligations of the commercial relationship is to be performed or the place with which the subject-matter of the dispute is most closely con-nected; or

(c) the parties have expressly agreed that the subject matter of the arbitration agreement relates to more than one country.

Article 2: Deûnitions

(a) “arbitration” means any arbitration whether or not administered by a permanent arbitral institution;

(b) “arbitral tribunal” means a sole arbitrator or a panel of arbitrators;

(c) “court” means a body or organ of the judicial system of a State;

Article 3. Receipt of written communications

(1) Unless otherwise agreed by the parties:

(a) any written communication is deemed to have been received if it is delivered to the addressee personally or if it is delivered at his place of business, habitual residence or mailing address; if none of these can be found after making a reasonable inquiry, a written communication is deemed to have been received if it

is sent to the addressee's last-known place of busi-ness, habitual residence or mailing address by registered letter or any other means which provides a record of the attempt to deliver it;

(b) the communication is deemed to have been received on the day it is so delivered.

(2) The provisions of this article do not apply to communications in court proceedings.

Article 4. Waiver of right to object

A party who knows that any provision of this Law from which the parties may derogate or any requirement under the arbitration agreement has not been complied with and yet proceeds with the arbitration without stating his objection to such non-compliance without undue delay or, if a time-limit is provided therefor, within such period of time, shall be deemed to have waived his right to object.

Article 5. Extent of court intervention

In matters governed by this Law, no court shall intervene except where so provided in this Law.

Article 6. Court or other authority for certain functions of arbitration assistance and supervision

The functions referred to in articles 11(3), 11(4), 13(3), 14, 16(3) and 34(2) shall be performed by ... [Each State enacting this model law speciû es the court, courts or, where referred to therein, other authority competent to perform these functions.]

Article 7. Deûnition and form of arbitration agreement

(1) "Arbitration agreement" is an agreement by the parties to submit to arbitration all or certain disputes which have arisen or which may arise between them in respect of a deûned legal relationship, whether contractual or not. An arbitration agreement may be in the form of an arbitration clause in a contract or in the form of a separate agreement.

(2) The arbitration agreement shall be in writing.

(3) An arbitration agreement is in writing if its content is recorded in any form, whether or not the arbitration agreement or contract has been con-cluded orally, by conduct, or by other means.

(4) The requirement that an arbitration agreement be in writing is met by an electronic communication if the information contained therein is acces-sible so as to be useable for subsequent reference; "electronic communica-tion" means any communication that the parties make by means of data messages; "data message" means information generated, sent, received or stored by electronic, magnetic, optical or similar means, including, but not limited to, electronic data interchange (EDI), electronic mail, telegram, telex or telecopy.

(5) Furthermore, an arbitration agreement is in writing if it is contained in an exchange of statements of claim and defence in which the existence of an agreement is alleged by one party and not denied by the other.

(6) The reference in a contract to any document containing an arbitration clause constitutes an arbitration agreement in writing, provided that the ref-erence is such as to make that clause part of the contract.

or

"Arbitration agreement" is an agreement by the parties to submit to arbitra-tion all or certain disputes which have arisen or which may arise between them in respect of a deûned legal relationship, whether contractual or not.

Article 8. Arbitration agreement and substantive claim before court

(1) A court before which an action is brought in a matter which is the subject of an arbitration agreement shall, if a party so requests not later than when submitting his ûrst statement on the substance of the dispute, refer the parties to arbitration unless it ûnds that the agreement is null and void, inoperative or incapable of being performed.

(2) Where an action referred to in paragraph (1) of this article has been brought, arbitral proceedings may

nevertheless be commenced or continued, and an award may be made, while the issue is pending before the court.

Article 9. Arbitration agreement and interim measures by court

It is not incompatible with an arbitration agreement for a party to request, before or during arbitral proceedings, from a court an interim measure of protection and for a court to grant such measure.

Article 10. Number of arbitrators

(1) The parties are free to determine the number of arbitrators.

(2) Failing such determination, the number of arbitrators shall be three.

Article 11. Appointment of arbitrators

(1) No person shall be precluded by reason of his nationality from acting as an arbitrator, unless otherwise agreed by the parties.

(2) The parties are free to agree on a procedure of appointing the arbitrator or arbitrators, subject to the provisions of paragraphs (4) and (5) of this article.

(3) Failing such agreement,

(a) in an arbitration with three arbitrators, each party shall appoint one arbitrator, and the two arbitrators thus appointed shall appoint the third arbitrator; if a party fails to appoint the arbitrator within thirty days of receipt of a request to do so from the other party, or if the two arbitrators fail to agree on the third arbitrator within thirty days of their appointment, the appointment shall be made, upon request of a party, by the court or other authority speciûed in article 6;

(b) in an arbitration with a sole arbitrator, if the parties are unable to agree on the arbitrator, he shall be appointed, upon request of a party, by the court or other authority speciûed in article 6.

(4) Where, under an appointment procedure agreed upon by the parties,

(a) a party fails to act as required under such procedure, or

(b) the parties, or two arbitrators, are unable to reach an agreement expected of them under such procedure, or

(c) a third party, including an institution, fails to perform any function entrusted to it under such procedure, any party may request the court or other authority speciûed in article 6 to take the necessary measure, unless the agreement on the appointment pro-cedure provides other means for securing the appointment.

(5) A decision on a matter entrusted by paragraph (3) or (4) of this article to the court or other authority speciûed in article 6 shall be subject to no appeal. The court or other authority, in appointing an arbitrator, shall have due regard to any qualiûcations required of the arbitrator by the agreement of the parties and to such considerations as are likely to secure the appoint-ment of an independent and impartial arbitrator and, in the case of a sole or third arbitrator, shall take into account as well the advisability of appoint-ing an arbitrator of a nationality other than those of the parties.

Article 12. Grounds for challenge

(1) When a person is approached in connection with his possible appoint-ment as an arbitrator, he shall disclose any circumstances likely to give rise to justiûable doubts as to his impartiality or independence. An arbitrator, from the time of his appointment and throughout the arbitral proceedings, shall without delay disclose any such circumstances to the parties unless they have already been informed of them by him.

(2) An arbitrator may be challenged only if circumstances exist that give rise to justiûable doubts as to his impartiality or independence, or if he does not possess qualiû cations agreed to by the parties. A party may

challenge an arbitra-tor appointed by him, or in whose appointment he has participated, only for reasons of which he becomes aware after the appointment has been made.

Article 13. Challenge procedure

(1) The parties are free to agree on a procedure for challenging an arbitra-tor, subject to the provisions of paragraph (3) of this article.

(2) Failing such agreement, a party who intends to challenge an arbitrator shall, within ûfteen days after becoming aware of the constitution of the arbitral tribunal or after becoming aware of any circumstance referred to in article 12(2), send a written statement of the reasons for the challenge to the arbitral tribunal. Unless the challenged arbitrator withdraws from his ofûce or the other party agrees to the challenge, the arbitral tribunal shall decide on the challenge.

(3) If a challenge under any procedure agreed upon by the parties or under the procedure of paragraph (2) of this article is not successful, the challeng-ing party may request, within thirty days after having received notice of the decision rejecting the challenge, the court or other authority speciû ed in article 6 to decide on the challenge, which decision shall be subject to no appeal; while such a request is pending, the arbitral tribunal, including the challenged arbitrator, may continue the arbitral proceedings and make an award.

Article 14. Failure or impossibility to act

(1) If an arbitrator becomes *de jure* or *de facto* unable to perform his func-tions or for other reasons fails to act without undue delay, his mandate terminates if he withdraws from his ofûce or if the parties agree on the termination. Otherwise, if a controversy remains concerning any of these grounds, any party may request the court or other authority speciû ed in article 6 to decide on the termination of the mandate, which decision shall be subject to no appeal.

(2) If, under this article or article 13(2), an arbitrator withdraws from his ofûce or a party agrees to the termination of the mandate of an arbitrator, this does not imply acceptance of the validity of any ground referred to in this article or article 12(2).

Article 15. Appointment of substitute arbitrator

Where the mandate of an arbitrator terminates under article 13 or 14 or because of his withdrawal from ofûce for any other reason or because of the revocation of his mandate by agreement of the parties or in any other case of termination of his mandate, a substitute arbitrator shall be appointed according to the rules that were applicable to the appointment of the arbitra-tor being replaced.

Article 16. Competence of arbitral tribunal to rule on its jurisdiction

(1) The arbitral tribunal may rule on its own jurisdiction, including any objections with respect to the existence or validity of the arbitration agree-ment. For that purpose, an arbitration clause which forms part of a contract shall be treated as an agreement independent of the other terms of the con-tract. A decision by the arbitral tribunal that the contract is null and void shall not entail *ipso jure* the invalidity of the arbitration clause.

(2) A plea that the arbitral tribunal does not have jurisdiction shall be raised not later than the submission of the statement of defence. A party is not precluded from raising such a plea by the fact that he has appointed, or participated in the appointment of, an arbitrator. A plea that the arbitral tri-bunal is exceeding the scope of its authority shall be raised as soon as the matter alleged to be beyond the scope of its authority is raised during the arbitral proceedings. The arbitral tribunal may, in either case, admit a later plea if it considers the delay justiû ed.

(3) The arbitral tribunal may rule on a plea referred to in paragraph (2) of this article either as a preliminary question or in an award on the merits. If the arbitral tribunal rules as a preliminary question that it has jurisdiction, any party may request, within thirty days after having received notice of that ruling, the court speciûed in article 6 to decide the matter, which deci-sion shall be subject to no appeal; while such a request is pending, the arbitral tribunal may continue the arbitral proceedings and make an award.

Article 17. Power of arbitral tribunal to order interim measures

(1) Unless otherwise agreed by the parties, the arbitral tribunal may, at the request of a party, grant interim measures.

(2) An interim measure is any temporary measure, whether in the form of an award or in another form, by which, at any time prior to the issuance of the award by which the dispute is ûnally decided, the arbitral tribunal orders a party to:

(a) Maintain or restore the status quo pending determination of the dispute;

(b) Take action that would prevent, or refrain from taking action that is likely to cause, current or imminent harm or prejudice to the arbitral process itself;

(c) Provide a means of preserving assets out of which a subsequent award may be satisû ed; or

(d) Preserve evidence that may be relevant and material to the resolu-tion of the dispute.

Article 17 A. Conditions for granting interim measures

(1) The party requesting an interim measure under article 17(2)*(a)*, *(b)* and

(c) shall satisfy the arbitral tribunal that:

(a) Harm not adequately reparable by an award of damages is likely to result if the measure is not ordered, and such harm substantially outweighs the harm that is likely to result to the party against whom the measure is directed if the measure is granted; and

(b) There is a reasonable possibility that the requesting party will succeed on the merits of the claim. The determination on this possibility shall not affect the discretion of the arbitral tribunal in making any subse-quent determination.

(2) With regard to a request for an interim measure under article 17(2)*(d)*, the requirements in paragraphs (1)*(a)* and *(b)* of this article shall apply only to the extent the arbitral tribunal considers appropriate.

Article 17 B. Applications for preliminary orders and conditions for granting preliminary orders

(1) Unless otherwise agreed by the parties, a party may, without notice to any other party, make a request for an interim measure together with an application for a preliminary order directing a party not to frustrate the purpose of the interim measure requested.

(2) The arbitral tribunal may grant a preliminary order provided it considers that prior disclosure of the request for the interim measure to the party against whom it is directed risks frustrating the purpose of the measure.

(3) The conditions deûned under article 17A apply to any preliminary order, provided that the harm to be assessed under article 17A(1)*(a)*, is the harm likely to result from the order being granted or not.

(1) Immediately after the arbitral tribunal has made a determination in respect of an application for a preliminary order, the arbitral tribunal shall give notice to all parties of the request for the interim measure, the application for

the preliminary order, the preliminary order, if any, and all other communi-cations, including by indicating the content of any oral communication, be-tween any party and the arbitral tribunal in relation thereto.

(2) At the same time, the arbitral tribunal shall give an opportunity to any party against whom a preliminary order is directed to present its case at the earliest practicable time.

(3) The arbitral tribunal shall decide promptly on any objection to the preliminary order.

(4) A preliminary order shall expire after twenty days from the date on which it was issued by the arbitral tribunal. However, the arbitral tribunal may issue an interim measure adopting or modifying the preliminary order, after the party against whom the preliminary order is directed has been given notice and an opportunity to present its case.

(5) A preliminary order shall be binding on the parties but shall not be subject to enforcement by a court. Such a preliminary order does not con-stitute an award.

Article 17 C. Speciûc regime for preliminary orders

The arbitral tribunal may modify, suspend or terminate an interim measure or a preliminary order it has granted, upon application of any party or, in exceptional circumstances and upon prior notice to the parties, on the arbitral tribunal's own initiative.

Article 17 E. Provision of security

(1) The arbitral tribunal may require the party requesting an interim measure to provide appropriate security in connection with the measure.

(2) The arbitral tribunal shall require the party applying for a preliminary order to provide security in connection with the order unless the arbitral tribunal considers it inappropriate or unnecessary to do so.

Article 17 F. Disclosure

(1) The arbitral tribunal may require any party promptly to disclose any material change in the circumstances on the basis of which the measure was requested or granted.

(2) The party applying for a preliminary order shall disclose to the arbitral tribunal all circumstances that are likely to be relevant to the arbitral tribu-nal's determination whether to grant or maintain the order, and such obliga-tion shall continue until the party against whom the order has been requested has had an opportunity to present its case. Thereafter, paragraph (1) of this article shall apply.

Article 17 G. Costs and damages

The party requesting an interim measure or applying for a preliminary order shall be liable for any costs and damages caused by the measure or the order to any party if the arbitral tribunal later determines that, in the circumstances, the measure or the order should not have been granted. The arbitral tribunal may award such costs and damages at any point during the proceedings.

Article 17 H. Recognition and enforcement

(1) An interim measure issued by an arbitral tribunal shall be recognized as binding and, unless otherwise provided by the arbitral tribunal, enforced upon application to the competent court, irrespective of the country in which it was issued, subject to the provisions of article 17 I.

(2) The party who is seeking or has obtained recognition or enforcement of an interim measure shall promptly inform the court of any termination, suspension or modiûcation of that interim measure.

(3) The court of the State where recognition or enforcement is sought may, if it considers it proper, order the requesting party to provide appropriate security if the arbitral tribunal has not already made a determination with respect to security or where such a decision is necessary to protect the rights of third parties.

Article 17 I. Grounds for refusing recognition or enforcement

(1) Recognition or enforcement of an interim measure may be refused only:

(a) At the request of the party against whom it is invoked if the court is satisûed that:

(i) Such refusal is warranted on the grounds set forth in arti-cle 36(1)*(a)*(i), (ii), (iii) or (iv); or

(ii) The arbitral tribunal's decision with respect to the provision of security in connection with the interim measure issued by the arbitral tribunal has not been complied with; or

(iii) The interim measure has been terminated or suspended by the arbitral tribunal or, where so empowered, by the court of the State in which the arbitration takes place or under the law of which

that interim measure was granted; or

(b) If the court ûnds that:

(i) The interim measure is incompatible with the powers con-ferred upon the court unless the court decides to reformulate the interim measure to the extent necessary to adapt it to its own powers and procedures for the purposes of enforcing that interim measure and without modifying its substance; or

(ii) Any of the grounds set forth in article 36(1)*(b)*(i) or (ii), apply to the recognition and enforcement of the interim measure.

(2) Any determination made by the court on any ground in paragraph (1) of this article shall be effective only for the purposes of the application to recognize and enforce the interim measure. The court where recognition or enforcement is sought shall not, in making that determination, undertake a review of the substance of the interim measure.

Article 17 J. Court-ordered interim measures

A court shall have the same power of issuing an interim measure in relation to arbitration proceedings, irrespective of whether their place is in the territory of this State, as it has in relation to proceedings in courts. The court shall exercise such power in accordance with its own procedures in consideration of the speciûc features of international arbitration.

Article 18. Equal treatment of parties

The parties shall be treated with equality and each party shall be given a full opportunity of presenting his case.

Article 19. Determination of rules of procedure

(1) Subject to the provisions of this Law, the parties are free to agree on the procedure to be followed by the arbitral tribunal in conducting the proceedings.

(2) Failing such agreement, the arbitral tribunal may, subject to the provi-sions of this Law, conduct the arbitration in such manner as it considers appropriate. The power conferred upon the arbitral tribunal includes the power to determine the admissibility, relevance, materiality and weight of any evidence.

Article 20. Place of arbitration

(1) The parties are free to agree on the place of arbitration. Failing such agreement, the place of arbitration shall be determined by the arbitral tribunal having regard to the circumstances of the case, including the convenience of the parties.

(2) Notwithstanding the provisions of paragraph (1) of this article, the arbi-tral tribunal may, unless otherwise agreed by the parties, meet at any place it considers appropriate for consultation among its members, for hearing witnesses, experts or the parties, or for inspection of goods, other property or documents.

Article 21. Commencement of arbitral proceedings

Unless otherwise agreed by the parties, the arbitral proceedings in respect of a particular dispute commence on the date on which a request for that dispute to be referred to arbitration is received by the respondent.

Article 22. Language

(1) The parties are free to agree on the language or languages to be used in the arbitral proceedings. Failing such agreement, the arbitral tribunal shall determine the language or languages to be used in the proceedings. This agreement or determination, unless otherwise speciûed therein, shall apply to any written statement by a party, any hearing and any award, decision or other communication by the arbitral tribunal.

(2) The arbitral tribunal may order that any documentary evidence shall be accompanied by a translation into the language or languages agreed upon by the parties or determined by the arbitral tribunal.

Article 23. Statements of claim and defence

(1) Within the period of time agreed by the parties or determined by the arbitral tribunal, the claimant shall state the facts supporting his claim, the points at issue and the relief or remedy sought, and the respondent shall state his defence in respect of these particulars, unless the parties have other-wise agreed as to the required elements of such statements. The parties may submit with their statements all documents they consider to be relevant or may add a reference to the documents or other evidence they will submit.

(2) Unless otherwise agreed by the parties, either party may amend or supplement his claim or defence during the course of the arbitral proceed-ings, unless the arbitral tribunal considers it inappropriate to allow such amendment having regard to the delay in making it.

Article 24. Hearings and written proceedings

(1) Subject to any contrary agreement by the parties, the arbitral tribunal shall decide whether to hold oral hearings for the presentation of evidence or for oral argument, or whether the proceedings shall be conducted on the basis of documents and other materials. However, unless the parties have agreed that no hearings shall be held, the arbitral tribunal shall hold such hearings at an appropriate stage of the proceedings, if so requested by a party.

(2) The parties shall be given sufûcient advance notice of any hearing and of any meeting of the arbitral tribunal for the purposes of inspection of goods, other property or documents.

(3) All statements, documents or other information supplied to the arbitral tribunal by one party shall be communicated to the other party. Also any expert report or evidentiary document on which the arbitral tribunal may rely in making its decision shall be communicated to the parties.

Article 25. Default of a party

Unless otherwise agreed by the parties, if, without showing sufû cient cause,

(a) the claimant fails to communicate his statement of claim in accordance with article 23(1), the arbitral tribunal shall terminate the proceedings;

(b) the respondent fails to communicate his statement of defence in accordance with article 23(1), the arbitral tribunal shall continue the proceed-ings without treating such failure in itself as an admission of the claimant's allegations;

(c) any party fails to appear at a hearing or to produce documentary evidence, the arbitral tribunal may continue the proceedings and make the award on the evidence before it.

Article 26. Expert appointed by arbitral tribunal

(1) Unless otherwise agreed by the parties, the arbitral tribunal

(a) may appoint one or more experts to report to it on speciû c issues to be determined by the arbitral tribunal;

(b) may require a party to give the expert any relevant information or to produce, or to provide access to, any relevant documents, goods or other property for his inspection.

(2) Unless otherwise agreed by the parties, if a party so requests or if the arbitral tribunal considers it necessary, the expert shall, after delivery of his written or oral report, participate in a hearing where the parties have the opportunity to put questions to him and to present expert witnesses in order to testify on the points at issue.

Article 27. Court assistance in taking evidence

The arbitral tribunal or a party with the approval of the arbitral tribunal may request from a competent court of this State assistance in taking evidence.

The court may execute the request within its competence and according to its rules on taking evidence.

Article 28. Rules applicable to substance of dispute

(1) The arbitral tribunal shall decide the dispute in accordance with such rules of law as are chosen by the parties as applicable to the substance of the dispute. Any designation of the law or legal system of a given State shall be construed, unless otherwise expressed, as directly referring to the substantive law of that State and not to its conûict of laws rules.

(2) Failing any designation by the parties, the arbitral tribunal shall apply the law determined by the conûict of laws rules which it considers applicable.

(3) The arbitral tribunal shall decide *ex aequo et bono* or as *amiable com-positeur* only if the parties have expressly authorized it to do so.

(4) In all cases, the arbitral tribunal shall decide in accordance with the terms of the contract and shall take into account the usages of the trade applicable to the transaction.

Article 29. Decision-making by panel of arbitrators

In arbitral proceedings with more than one arbitrator, any decision of the arbitral tribunal shall be made, unless otherwise agreed by the parties, by a majority of all its members. However, questions of procedure may be decided by a presiding arbitrator, if so authorized by the parties or all members of the arbitral tribunal.

Article 30. Settlement

(1) If, during arbitral proceedings, the parties settle the dispute, the arbitral tribunal shall terminate the proceedings and, if requested by the parties and not objected to by the arbitral tribunal, record the settlement in the form of an arbitral award on agreed terms.

(2) An award on agreed terms shall be made in accordance with the provi-sions of article 31 and shall state that it is an award. Such an award has the same status and effect as any other award on the merits of the case.

Article 31. Form and contents of award

(1) The award shall be made in writing and shall be signed by the arbitra-tor or arbitrators. In arbitral proceedings with more than one arbitrator, the signatures of the majority of all members of the arbitral tribunal shall sufûce, provided that the reason for any omitted signature is stated.

(2) The award shall state the reasons upon which it is based, unless the parties have agreed that no reasons are to be given or the award is an award on agreed terms under article 30.

(3) The award shall state its date and the place of arbitration as determined in accordance with article 20(1). The award shall be deemed to have been made at that place.

(4) After the award is made, a copy signed by the arbitrators in accordance with paragraph (1) of this article shall be delivered to each party.

Article 32. Termination of proceedings

(1) The arbitral proceedings are terminated by the ûnal award or by an order of the arbitral tribunal in accordance with paragraph (2) of this article.

(2) The arbitral tribunal shall issue an order for the termination of the arbi-tral proceedings when:

(a) the claimant withdraws his claim, unless the respondent objects thereto and the arbitral tribunal recognizes

a legitimate interest on his part in obtaining a ûnal settlement of the dispute;

(b) the parties agree on the termination of the proceedings;

(c) the arbitral tribunal ûnds that the continuation of the proceedings has for any other reason become unnecessary or impossible.

(3) The mandate of the arbitral tribunal terminates with the termination of the arbitral proceedings, subject to the provisions of articles 33 and 34(4).

Article 33. Correction and interpretation of award; additional award

(1) Within thirty days of receipt of the award, unless another period of time has been agreed upon by the parties:

(a) a party, with notice to the other party, may request the arbitral tribunal to correct in the award any errors in computation, any clerical or typographical errors or any errors of similar nature;

(b) if so agreed by the parties, a party, with notice to the other party, may request the arbitral tribunal to give an interpretation of a speciû c point or part of the award. If the arbitral tribunal considers the request to be justiûed, it shall make the correction or give the interpretation within thirty days of receipt of the request. The interpretation shall form part of the award.

(2) The arbitral tribunal may correct any error of the type referred to in paragraph (1)*(a)* of this article on its own initiative within thirty days of the date of the award.

(3) Unless otherwise agreed by the parties, a party, with notice to the other party, may request, within thirty days of receipt of the award, the arbitral tribunal to make an additional award as to claims presented in the arbitral proceedings but omitted from the award. If the arbitral tribunal considers the request to be justiûed, it shall make the additional award within sixty days.

(4) The arbitral tribunal may extend, if necessary, the period of time within which it shall make a correction, interpretation or an additional award under paragraph (1) or (3) of this article.

(5) The provisions of article 31 shall apply to a correction or interpretation of the award or to an additional award.

Article 34. Application for setting aside as exclusive recourse against arbitral award

(1) Recourse to a court against an arbitral award may be made only by an application for setting aside in accordance with paragraphs (2) and (3) of this article.

(2) An arbitral award may be set aside by the court speciûed in article 6 only if:

(a) the party making the application furnishes proof that:

(i) a party to the arbitration agreement referred to in article 7 was under some incapacity; or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of this State; or

(ii) the party making the application was not given proper notice of the appointment of an arbitrator or of the arbitral proceed-ings or was otherwise unable to present his case; or

(iii) the award deals with a dispute not contemplated by or not fall-ing within the terms of the submission to arbitration, or contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, only that part of the award which contains decisions on matters not submitted to arbitration may be set aside; or

(iv) the composition of the arbitral tribunal or the arbitral proce-dure was not in accordance with the agreement of the parties, unless such agreement was in conûict with a provision of this Law from

which the parties cannot derogate, or, failing such agreement, was not in accordance with this Law; or

(b) the court û nds that:

(i) the subject-matter of the dispute is not capable of settlement by arbitration under the law of this State; or

(ii) the award is in conûict with the public policy of this State.

(3) An application for setting aside may not be made after three months have elapsed from the date on which the party making that application had received the award or, if a request had been made under article 33, from the date on which that request had been disposed of by the arbitral tribunal.

(4) The court, when asked to set aside an award, may, where appropriate and so requested by a party, suspend the setting aside proceedings for a period of time determined by it in order to give the arbitral tribunal an opportunity to resume the arbitral proceedings or to take such other action as in the arbitral tribunal's opinion will eliminate the grounds for setting aside.

Article 35. Recognition and enforcement

(1) An arbitral award, irrespective of the country in which it was made, shall be recognized as binding and, upon application in writing to the competent court, shall be enforced subject to the provisions of this article and of article 36.

(2) The party relying on an award or applying for its enforcement shall supply the original award or a copy thereof. If the award is not made in an ofûcial language of this State, the court may request the party to supply a translation thereof into such language.[4]

Article 36. Grounds for refusing recognition or enforcement

(1) Recognition or enforcement of an arbitral award, irrespective of the country in which it was made, may be refused only:

(a) at the request of the party against whom it is invoked, if that party furnishes to the competent court where recognition or enforcement is sought proof that:

(i) a party to the arbitration agreement referred to in article 7 was under some incapacity; or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of the country where the award was made; or

(ii) the party against whom the award is invoked was not given proper notice of the appointment of an arbitrator or of the arbitral proceedings or was otherwise unable to present his case; or

(iii) the award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, that part of the award which contains deci-sions on matters submitted to arbitration may be recognized and enforced; or

(iv) the composition of the arbitral tribunal or the arbitral proce-dure was not in accordance with the agreement of the parties or, failing such agreement, was not in accordance with the law of the country where the arbitration took place; or

(v) the award has not yet become binding on the parties or has been set aside or suspended by a court of the country in which, or under the law of which, that award was made; or

(b) if the court ûnds that:

(i) the subject-matter of the dispute is not capable of settlement by arbitration under the law of this State; or

(ii) the recognition or enforcement of the award would be contrary to the public policy of this State.

(2) If an application for setting aside or suspension of an award has been made to a court referred to in paragraph (1)*(a)*(v) of this article, the court where recognition or enforcement is sought may, if it considers it proper, adjourn its decision and may also, on the application of the party claiming recognition or enforcement of the award, order the other party to provide appropriate security.

LESSON ROUND UP

- Foreign collaboration is such an alliance of domestic (native) and foreign (non-native) entities like individuals, firms, companies, organizations, governments, etc., that come together with an intention to finalize a contract on some tasks or jobs or projects
- In case of financial collaboration, the inflow of foreign investment takes place in the domestic (host) country. In case of technical collaboration, the inflow of foreign technology takes place in the domestic (host) country.
- In case of marketing collaboration, the inflow of foreign goods and services take place in the domestic (host) country.
- In case of management consultancy collaboration, the inflow of foreign management consultancy takes place in the domestic (host) country.
- In India there are basically two forms of foreign collaboration. The collaboration may be either financial collaboration or it may be technical.
- A joint venture is an association of two or more individuals or business entities who combine and pool their respective expertise, financial resources, skills, experience, and knowledge in the furtherance of a particular project or undertaking.
- Joint Ventures are generally created for a single activity or project, and may have a limited time span. Joint Venture agreements, commonly referred to as a “JV”, are typically formed either by individuals, business entities, corporations or partnerships.
- The contributions to the joint ventures are either in the form of money [capital], services, or physical asset(s), i.e. equipment or intellectual property [software, patents], etc., or a combination of all.
- The investments in Joint Ventures (JV) and Wholly Owned Subsidiaries (WOS) abroad have been recognized as important avenues for promoting global business by Indian entrepreneurs in terms of foreign exchange earnings like dividend, royalty, technical know-how fee and other entitlements on such investments.
- There are two fundamental types of joint venture, i.e., Equity Joint Venture and Contractual Joint Venture
- The equity joint venture is an arrangement whereby a separate legal entity is created in accordance with the agreement of two or more parties.
- The contractual joint venture might be used where the establishment of a separate legal entity is not needed or the creation of such a separate legal entity is not feasible in view of one or the other reasons.
- The joint venture agreement forms the basis of the understanding between and among the parties. It is relied upon to ensure that all parties understand their roles, rights, responsibilities, and remedies in the conduct of the venture.

- A key to developing joint venture agreements is to determine goals and objectives in advance and ensure that the interests are reflected in the agreement.
- "International Commercial Arbitration" is a particular means of settling disputes, i.e. by "arbitration" that is "commercial" in nature and has some international element to it.

SELF TEST QUESTIONS

1. Explain the meaning and features of foreign collaboration.
2. Describe the procedure in detail for forming foreign technology collaboration in India.
3. What is meant by the term 'Joint Venture'? Explain types of join venture.
4. You are a Company Secretary of ABC Limited which is planning to enter into joint venture with XYZ Limited based in Singapore for marketing and selling a new product launched by your company. As a company secretary please advice your company what are the issues which need to be dealt while negotiating a Joint Venture agreement.
5. What are the factors to consider while drafting a joint venture agreement?
6. A foreign company 'Cuba Limited' wants to render technical services to the Indian company 'Puma Limited'. Draft a specimen foreign collaboration agreement for the same.
7. Discuss international commercial arbitration as an important tool of dispute settlement in foreign collaborations.

Lesson 11
Strategic Alliances

LESSON OUTLINE

– Introduction
– Meaning and Definition
– Advantages of Strategic Alliances
– Disadvantages of Strategic Alliances
– Types of Strategic Alliances
– Stages of Alliance Formation
– Reasons for Creating Strategic Alliances
– Managing Strategic Alliances
– Critical success factors
– Strategic Alliance Failures
– Alliances Checklist
– Trends in Strategic Alliances
– LESSON ROUND UP
– SELF TEST QUESTIONS

LEARNING OBJECTIVES

Strategic alliances among international business are very common. Globalization of the business is the order of the day. But internationalization can be very expensive process, particularly where a firm must coordinate Research & Development, production, marketing, human resources and financial decisions to succeed. It is generally short of all these resources. Therefore it may seek a partner to share these costs. For example a firm may develop a new technology but lacks resources for its marketing. So it can enter into the strategic alliance with some other company which is good at marketing functions. Such alliance is strategic alliance.

A global strategic alliance is usually established when a company wishes to edge into a related business or new geographic market — particularly one where the government prohibits imports in order to protect domestic industry. Typically, alliances are formed between two or more corporations, each based in their home country, for a specified period of time. Their purpose is to share ownership of a newly formed venture and maximize competitive advantages in their combined territories.

In this chapter we will study what are strategic alliances, their advantages and disadvantages, how to form strategic alliances and managing alliances in global economy.

"Alliances have become an integral part of contemporary strategic thinking." Fortune Magazine

"Partnering is the quickest, most effective way to re-engineer a business." Curtis E. Sahakian

Strategic Alliances: A Key Element of the Toshiba's Corporate Strategy

Toshiba firmly believes that a single company cannot dominate any technology or business by itself. Toshiba's approach is to develop synergistic relationships with different partners for different technologies. Strategic alliances form a key element of Toshiba's corporate strategy. They helped the company to become one of the leading players in the global electronics industry. In early 1990s Toshiba signed a coproduction agreement for light bulb filaments with GE. Jack Welch, the legendary former CEO of GE, was a Toshiba's admirer. According to him, a phone call to Japan was enough to sort out problems if and when they arise, in no time. Since then, Toshiba formed various partnerships, technology licensing agreements and joint ventures. Toshiba's alliance partners include Apple Computers, Ericsson, GE, IBM, Microsoft, Motorola, National Semi Conductor, Samsung, Siemens, Sun Microsystems and Thomson.

Toshiba formed an alliance with Apple Computer to develop multimedia computer products. Apple's strength lay in software technology, while Toshiba contributed its manufacturing expertise. Toshiba created a similar tie-up with Microsoft for hand held computer systems.

In semiconductors, Toshiba, IBM and Siemens came together to pool different types of skills. Toshiba was strong in etching, IBM in lithography and Siemens in engineering. The understanding among the partners was limited to research. For commercial production and marketing the partners decided to be on their own.

In flash memory, Toshiba formed alliances with IBM and National Semi Conductor. Toshiba's alliance with Motorola has helped it become a world leader in the production of memory chips. The tie-up with IBM has enabled Toshiba to become a world's largest supplier of color flat panel displays for notebooks.

Toshiba believes in a flexible approach because some tension is natural in business partnerships, some of which may also sour over time. Toshiba executives believe that the relationship between the company and its partner should be like friends, not like that of a married couple. Toshiba senior management is often directly involved in the management of strategic alliances. This helps in building personal equations and resolving conflicts.

INTRODUCTION

Nike, the largest producer of athletic foot wear in the world, does not manufacture a single shoe. Gallo, the largest wine company on earth, does not grow a single grape. You may ask "How can this be?". These companies, like many other companies these days, have entered into strategic alliances with their suppliers to do much of their actual production and manufacturing for them.

A strategic alliance is an agreement between firms to do business together in ways that go beyond normal company-to-company dealings, but fall short of a merger or a full partnership. These alliances range from informal handshake agreements to formal agreements with lengthy contracts in which the parties may also exchange equity, or contribute capital to form a joint venture corporation.

Strategic alliances had typically focused on alliances between two companies; however, there is an increasing trend towards multi-company alliances. As an example, a six-company strategic alliance was formed between Apple, Sony, Motorola, Philips, AT&T and Matsushita to form General Magic Corporation to develop Telescript communications software.

Alliances between companies have become a crucial weapon in the battle for competitive advantage. Mergers/acquisitions/strategic alliance can be termed as coalescing and are becoming more and more popular. A "strategic alliance" is an excellent vehicle for two companies to work together profitably. Managed wisely, a strategic alliance can help companies develop and exploit their unique strengths. Through strategic alliances, organizations get an opportunity to widen their customer base, offload or utilize their surplus capacity, integrate vertically, use each others strengths and so on. For example, a large company can break down the marketing barriers that

face a small company, which in turn brings entrepreneurial creativity to the partnership. An alliance can also be a powerful tool for accessing new technology and developing domestic or international business opportunities.

Corporate relationships are quite dynamic – an alliance that begins as a simple licensing agreement may blossom in time into a variety of technology sharing agreements, joint venture companies and cross equity shareholdings. Many companies form not only single partnerships but entire network of alliances. In general, alliances set no time limits. Their duration is a function of the objectives and structures of the partnership, the prevailing business conditions and the management capabilities of the partners.

Many organizations however do not have a clear vision of their long-term direction. They are propelled by short-term tactical or operational needs. Such companies are prone to enter into alliances simply because a potential partner approaches them with a proposal. Most of the "strategic alliances" do not result in additional business, capabilities, or profitability for either of the companies involved, because they have not been well planned in the first place, and/or implementation has been left to someone else.

Alliances are used to enter new markets, access new technologies and achieve economies of scale faster and cheaper than any other acquisition method. The recent trend of collaborations consist of alliances varying from joint ventures, licensing deals, research consortia and technological exchanges to supply agreements and marketing alliances.

However, strategic alliances are not simple or easy to create, develop, and support. The process of establishing and managing winning alliances starts with the crucial process of picking the right partner and creating realistic expectations on both sides. Firstly, the intent of both parties must be clearly established. Analyzing the corporate and individual personality types involved in an alliance can help managers forecast and avoid problems due to lack of communication or mismatched value systems.

Strategic alliances projects often fail because of tactical errors made by management. By using a well managed strategic alliances agreement, companies can gain in markets that would otherwise be uneconomical. Considerable time and energy must be put forth by all involved in order to create a successful alliance. It is essential that corporations enter into strategic alliances arrangements with a comprehensive plan outlining detailed expectations, requirements, and expected benefits.

MEANING AND DEFINITION

Any arrangement or agreement under which two or more firms cooperate in order to achieve certain commercial objectives is referred to as strategic alliance. A true strategic alliance is a written arrangement between two companies that complement each other in a particular identified area. It is not a partnership, and neither company has legal power to control or obligate the other. Instead, it is a commitment by the two companies to provide capabilities or cross servicing in certain identified areas.

Merriam-Webster Collegiate Dictionary, tenth edition defines alliances as "associations to further the common interests of the members" or "intercorporate agreements covering a wide gamut of functions ranging from component sourcing through research and development to production and marketing."

Basic definition: "A strategic alliance is a strategic cooperation between two or more organizations, with the aim to achieve a result one of the parties cannot (easily) achieve alone."

According to Yoshino (1995) Strategic alliance has three distinguishing characteristics:

- *the two or more firms that unite to pursue a set of agreed goals remain independent subsequent to the formation of an alliance.*
- *the partner firms share the benefits of the alliance and control over the performance of assigned tasks.*
- *the partner firms contribute on a continuing basis in one or more key strategic areas e.g. technology, products and so forth.*

By properly utilizing a strategic alliance, companies can expand their product and service offerings substantially, without the usual corresponding investment in staff, equipment, and facilities. Strategic alliances are motivated by considerations such as cost reduction, technology sharing, product development, market access etc., Strategic alliances have objectives similar to those of conventional acquisitions but such alliances can prove to be less expensive than acquisition, if they are structured properly. This is because if two or more companies pool their resources they can secure their joint objectives more easily and economically.

Strategic alliances can take a variety of forms, ranging from an arm's-length contract to a joint venture. But the core of a strategic alliance is an inter-firm co-operative relationship that enhances the effectiveness of the competitive strategies of the participating firms by the trading of mutually beneficial resources such as technologies, skills, etc. Strategic alliances encompass a wide range of inter-firm linkages, including joint ventures, minority equity investments, equity swaps, joint research and development, joint manufacturing, joint marketing, long-term sourcing agreements, shared distribution/services and standards-setting. However, mergers and acquisitions, overseas subsidiaries of multinational corporations, and franchising agreements are not classified as strategic alliances, since they do not involve independent firms with separate goals or call for continuous contribution of participating firms such as transfer of technology or skills between partners.

ADVANTAGES OF STRATEGIC ALLIANCES

There are many specific advantages of a global strategic alliance.

- Instant market access, or entry into a new market at least speed.
- Exploit new opportunities to strengthen position in a market where firm already has a foothold.
- Increase sales.
- Gain new skills and technology.
- Develop new products at a profit.
- Share fixed costs and resources.
- Enlarge distribution channels.
- Broaden business and political contact base.
- Gain greater knowledge of international customs and culture.
- Enhance image in the world marketplace.

DISADVANTAGES OF STRATEGIC ALLIANCE

There are also some inevitable disadvantage of strategic alliances which organisations must consider:

- Weaker management involvement or less equity stake.
- Fear of market insulation due to local partner's presence.
- Less efficient communication.
- Poor resource allocation.
- Difficult to keep objectives on target over time.
- Loss of control over important issues such as product quality, operating costs, employees, etc.

TYPES OF STRATEGIC ALLIANCES

Strategic alliances can be of various types depending upon the factors like capital commitment, type of industry, structure of organisation etc.

Strategic alliance on the basis of type of industry

(i) ***Horizontal strategic alliance*****:** Strategic alliance which is characterized by the collaboration between two or more firms in the same industry, e.g. the partnership between Sina Corp and Yahoo in order to offer online auction services in China.

(ii) ***Vertical strategic alliance***: Strategic alliance which is characterized by the collaboration between two or more firms along the vertical chain of industry. e.g. Caterpillar's provision of manufacturing services to Land Rover.

(iii) ***Intersectoral strategic alliance*****:** Strategic alliance characterized by the collaboration between two or more firms neither in the same industry nor related through the vertical chain, e.g. the cooperation of Toys "R" in US with McDonald's in Japan resulting in Toys "R" US stores with built-in McDonald's restaurants.

Strategic alliance on the basis of capital commitments

(i) ***Joint venture*** : A strategic alliance in which two or more firms create a legally independent company to share some of their resources and capabilities to develop a competitive advantage.

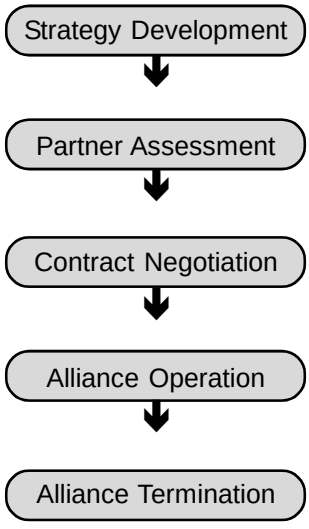
(ii) ***Equity strategic alliance*** : An alliance in which two or more firms own different percentages of the company they have formed by combining some of their resources and capabilities to create a competitive advantage.

(iii) **Non-equity strategic alliance** : An alliance in which two or more firms develop a contractual-relationship to share some of their unique resources and capabilities to create a competitive advantage.

(iv) ***Global Strategic Alliances*** : Working partnerships between companies (often more than two) across national boundaries and increasingly across industries, sometimes formed between company and a foreign government, or among companies and governments.

STAGES OF ALLIANCE FORMATION

A typical strategic alliance formation process involves these steps:



– **Strategy Development**: Strategy development involves studying the alliance's feasibility, objectives and rationale, focusing on the major issues and challenges and development of resource strategies for production, technology, and people. It requires aligning alliance objectives with the overall corporate strategy.

- **Partner Assessment**: Partner assessment involves analyzing a potential partner's strengths and weaknesses, creating strategies for accommodating partners' management styles, preparing appropriate partner selection criteria, understanding a partner's motives for joining the alliance and addressing resource capability gaps that may exist for a partner.
- **Contract Negotiation**: Contract negotiations involves determining whether all parties have realistic objectives, forming high calibre negotiating teams, defining each partner's contributions and rewards as well as protect any proprietary information, addressing termination clauses, penalties for poor performance, and highlighting the degree to which arbitration procedures are clearly stated and understood.
- **Alliance Operation**: Alliance operations involves addressing senior management's commitment, finding the calibre of resources devoted to the alliance, linking of budgets and resources with strategic priorities, measuring and rewarding alliance performance, and assessing the performance and results of the alliance.
- **Alliance Termination**: Alliance termination involves winding down the alliance, for instance when its objectives have been met or cannot be met, or when a partner adjusts priorities or re-allocates resources elsewhere.

REASONS FOR CREATING STRATEGIC ALLIANCES

Most firms enter into alliances out of need. According to an executive, "With alliances, we can do more for less". Whatever the needs driving alliance formation, managements must take the time to analyse why an alliance is the best strategy. The president of an automotive industry had once explained, "Understanding why you need a partnership is the most critical step. Sorting out the whys in the equation will in turn dictate the answers to key issues such as with whom you want to collaborate, how the partners will combine their strengths, and how the venture will be structured and managed." Some of the reasons for creating strategic alliances are given below:

(i) Growth strategies and entering new markets: In today's fast paced environment companies simply do not have the time to establish new markets one-by one. Therefore, forming an alliance with an existing company already in that marketplace is a very appealing alternative. Partnering with an international company can make the expansion into unfamiliar territory a lot easier and less stressful for a company.

(ii) Obtain new technology: All companies cannot provide the technology that they need to effectively compete in their markets on their own. Therefore, they can team up with other companies who do have the resources to provide the technology or who can pool their resources so that together they can provide the needed technology. Both sides receive benefit from the partnership. Technology transfer is viewed as being significant to the success of a strategic alliance.

(iii) Reduce cost by outsourcing: Another reason for forming strategic alliances is to outsource business functions, which can include, marketing, production, accounting, sales, or virtually any other process, to a company which can do it better and cheaper. Indeed, many companies are forming alliances looking for the best quality or technology, or the cheapest labor or production costs.

(iv) Reduce financial risk and share costs of research and development: Some companies may find that the financial risk that is involved in pursuing a new product or production method is too great for a single company to undertake. In such cases two or more companies agree to spread the risk among all of them.

(v) Achieve or ensure competitive advantage: Alliances are particularly alluring to small businesses because they provide the tools businesses need to be competitive. For many small companies the only way they can stay competitive and even survive in todays technologically advanced, ever-changing business world is to form an alliance with another company or companies. Small companies realize the mutual benefits they can derive from strategic alliances in areas such as marketing, distribution, production, research and

development, and outsourcing. By forming alliances with other companies, small businesses are able to accomplish bigger projects more quickly and profitably, than if they tried to do it on their own.

(vi) Knowledge transfer: Companies enter into alliances because there is knowledge required to create something new. An example here is the Senseo alliance between Philips and Sara Lee . Each of the parties was lacking the knowledge the other had. Philips is good in creating household appliances and Sara Lee knows all about coffee. Together they were able to bring a balanced coffeemaker to the market with dedicated Senseo coffee supplies.

(vii) Market development: Companies can enter into alliances to be able to develop new markets, whether it be geographic extensions or new market segments. In 1994 Pepsi and Starbucks entered into an alliance to bring bottled cold coffee drinks to the market. For both of them a complete new market was created that was diffcult for either of them to enter without the knowledge and capabilities of the other.

(viii) Effciency: Companies can also form strategic alliances to focus on cost reduction and increasing effciencies. Take for example the Rolls Royce jet engine division. They established in 2003 an alliance with several logistics partners to increase the overall value to Rolls Royce's customers. Coming from a traditional purchase relationship this partnership was transformative. The focus was no longer on selecting the supplier with the lowest price, but on the customer experience. Partners were also encouraged to collaborate amongst each other, thus optimizing the entire system rather than optimizing in silos as was done previously. This partnership led to an increase to 99% on time delivery and a 20% overall cost reduction without reducing partner profftability.

(ix) Satisfy customer demands: Customer demands in many markets are changing. For example, in office automation, customers now prefer a "systems solution" and want to rely on a single company to service all equipment. So, companies can enter into strategic alliances to satisfy new customer demands.

(x) Use excess capacity: A large number of companies have used the strategic alliances to soak up excess capacity of manufacturing units they have.

MANAGING STRATEGIC ALLIANCES

Managing an alliance is relatively a new art. Finding the right mix of management ingredients for success is quite daunting. However certain factors responsible for successful management of a strategic alliance are given below.

(1) Senior management commitment: The commitment of the senior management of all companies involved in a strategic alliance is a key factor in the alliance's ultimate success. Indeed, for alliances to be truly strategic they must have a significant impact on the companies overall strategic plans; and must therefore be formulated, implemented, managed, and monitored with the full commitment of senior management. Without senior management's commitment, alliances will not receive the resources they need. If senior management is not committed to alliances, adequate managerial resources, in addition to capital, production, marketing and labor resources, may not be assigned in order for alliances to accomplish their objectives. The biggest hurdle senior management has to overcome in committing itself to strategic alliances is management's own fear of a loss of control. Xerox is an example of a company which has demonstrated a high level of senior management commitment to strategic alliances. Xerox even has executives with titles such as Senior Vice President, Corporate Strategic Alliances and Vice President, Worldwide Alliances.

(**2) Similarity of management philosophies:** Companies should prefer to form partnerships with those companies whose management philosophies, strategies and ideas are most similar to their own. Indeed, differences in corporate partners' personalities, can often lead to tragic results. Misunderstandings and fightings between the senior management of the two organizations eventually lead to failure of strategic alliance. Therefore, in order to ensure the best chance of success, companies should either seek partners who do have similar management philosophies, or draft an alliance agreement that adequately addresses the differences, and provides for their resolution.

(**3**) **Effective and strong management team:** A McKinsey study found that 50 percent of alliance failures are due to poor management. The best strategy to grow via alliances may be to move slowly, and start with simple alliances and move towards more complex ones as alliance experience and talent is acquired. Hewlett-Packard and Lotus are corporations which have been cited as having strong alliance management. Hewlett-Packard's approach to alliances is very formal, well-organized and structured. Hewlett-Packard has developed a 400-page alliance binder with case histories, tool kits, checklists, policies, and procedures to help not only its alliance managers, but its middle managers as well, to more appropriately manage alliances and alliance relationships. Hewlett-Packard also has developed its own two-day strategic alliance training class, which over 700 of its managers have attended to date. Lotus likewise has a strong management team for its alliances.

(**4**) **Frequent performance feedback:** In order for strategic alliances to succeed, their performance must be continually assessed and evaluated against the short and long-term goals and objectives for the alliance. In order for the feedback monitoring system to be successful, it is important that the goals of the alliance be well-defined and measurable. In addition, benchmarks for alliance performance should be set to assist management in evaluating alliance results. In general, an alliance is successful if both partners achieve their objectives or by its long-term strategic value. Another measurement technique for strategic alliances is looking at the market share. Strategic alliances are very tough to measure and evaluate, but can be done with the help of understanding the form used and understanding the goals of the companies involved.

(**5**) **Clearly defined shared goals and objectives :** In forming a strategic alliance the question must be asked: 'How integrated will the alliance be with the parent organizations?' Some alliances are highly integrated with one or more of the parent organizations and share such resources as manufacturing facilities, management staff, and support functions like payroll, purchasing, and research and development. Conversely, others may be autonomous and independent from their parent organizations. Whatever the relationship between the two partners, the merging of separate corporate cultures in which the parent firms may have different, strategic intents can be difficult. It is extremely important that alliances are aligned with the company strategy. Top management must articulate a clear link between where it expects the industry's future profit pools, how to capture a larger share of those profits, and where, alliances fit in that plan.

(**6**) **Thorough planning :** Planning, commitment, and agreement are essential to the success of any relationship. The overall strategy for the alliance must be mutually developed. Key managing individuals and areas of focus for the alliance must be identified. The first step is to gain a clear understanding of the vision and values of each company. The next step is to gain agreement on the market conditions in the region of the world that the joint venture will be operating in. The next step is to clearly state the issues, strengths, and concerns of each organization. These initial steps allows the participants to bridge preliminary gaps of understanding at the onset of the process. During these initial fact finding meetings the partners can learn a great deal about their potential partner(s). The next step is to identify areas of common ground. Here is where commonality in the strategic direction among the partners can be identified. Next the partners need to define the internal and external value of the alliance. They will also need to agree on the strategic opportunities to mutually pursue. The final step in this planning process is to create a tactical plan to address the strategic targets . Thorough planning is one of the key ingredients to the successful formation of strategic alliances.

(**7**) **Clearly understood roles :** In forming strategic alliances the partners must have clearly understood roles. Questions must be answered concerning the role of each partner . It is crucial that this question of control is resolved before the alliance is formed. Some firms view strategic alliances as a second-best option that they would prefer to do. This attitude towards an alliance is problematic. Because of uncertainty and discomfort, the feeling is that these alliances must be closely managed and controlled so as not to get out of hand. If the partners in an alliance decide up front exactly what each partner's role is in the newly-formed business, then there is no misunderstanding or uncertainty as to how decisions will be made. In this way the relationship between the partners will be a much more amicable one.

(**8**) **International vision :** In order to succeed in an international strategic alliance, managers of firms must

incorporate a global strategic vision into their enterprise. In order to compete in the growing international market, it will be increasingly necessary for firms to cooperate on a global level and continually build international relationships which will facilitate the process of global competition.

(**9) Partner selection :** Partnership selection is perhaps the most important step in creating a successful alliance. A successful alliance requires the joining of two competent firms, seeking a similar goal and both intent on its success. The term 'competent firm' is relative to the involved parties' strategies, objectives and goal. A strategic alliance must be structured so that it is the intent of both parties that it will actually succeed. The process for partner selection is:

(1) state the firm's strategy;

(2) develop a partnership benchmark;

(3) eliminate undesirable business sectors;

(4) select promising business sectors; and

(5) select from potential candidates.

Having selected a partner, the alliance should be structured so that the firm's risks of giving too much away to the partner are reduced to an acceptable level.

(**10) Communication between partners – maintaining relationships :**As with any relationship, communication is an essential attribute for the alliance to be successful. Without effective communication between partners, it would be like any relationship which does not manifest good communication practices and will fail. The necessity for good communications in building and maintaining a strong strategic alliance relationship is best summed up by Ohmae: "An alliance is a lot like a marriage. There may be no formal contract. There is no buying and selling of equity. There are few, if any, rigidly binding provisions. It is a loose evolving kind of relationship. Sure, there are guidelines and expectations, but no one expects a precise, measured return on the initial commitment. Both partners bring to an alliance a faith that they will be stronger together than they would be separately. Both believe that each has unique skills and functional abilities the other likes. And both have to work diligently over time to make the union successful."

CRITICAL SUCCESS FACTORS FOR STRATEGIC ALLIANCES

The various factors potentially conducive to successful alliances are:

(1) Partnership should be based on an optimum balance of business strength and ownership amongst partners.

(2) The partners to alliance should bring in complementary skills, and capabilities to the alliance.

(3) Conflict of interests by virtue of market overlap should be minimal and avoided as far as possible.

(4) A degree of autonomy, strong leadership, continual commitment and support should be present.

(5) Alliance should be capable of building trust and confidence among partners.

(6) Sensitive and empathetic approach to be followed while dealing with divergence of management styles and corporate culture.

STRATEGIC ALLIANCE FAILURES

The trend in business world shows that strategic alliances have not always brought about the desired results. Most studies tend to focus more on the determinants of their success rather than for the reasons they fail. It is the risks and problems that need to be analyzed more fully to determine the true reasons why over 60 percent of strategic alliances fail. Following points explain some of the reasons for failure of strategic alliances.

(1) Clash of cultures: Cultural clash is probably one of the biggest problems that corporations in alliances face today. These cultural problems consist of language, egos, chauvinism, and different attitudes to business. Problems can be particularly acute between a publicly quoted American holding company, keenly focused on shareholders value, and Japanese partners who have different priorities. It is important for the companies that are working together to be able to communicate and understand each other well or they are doomed before they even start. After the communication is worked out the firms face the problems with operations. Different cultures operate in different ways. For example, US companies tend to evaluate performance on the basis of profit, market share, and specific financial benefits While Japanese companies focus more on quality aspects, customer benefits and value addition.

(**2) Lack of trust:** Risk sharing is the primary bonding tool in a partnership. What will happen if one company is successful and the other experiences a failure? A sense of commitment must be generated throughout the partnership. In many alliance cases one company will point the failure finger at the partnering company. Shifting the blame does not solve the problem, but increases the tension between the partnering companies and often leads to alliance ruin. Building trust is the most important and yet most difficult aspect of a successful alliance. Only people can trust each other, not the company. Therefore, alliances need to be formed to enhance trust between individuals. The companies must form the three forms of trust, which include responsibility, equality, and reliability. Many alliances have failed due to the lack of trust causing unsolved problems, lack of understanding, and despondent relationships.

(**3) Lack of clear goals and objectives:** In today's business world, many strategic alliances are formed for the wrong reasons. This leads to disaster in the future. Many companies enter into alliances to combat industry competitors. Corporate management feels this type of action deters competitors from focusing on their company. On the contrary, this action raises flags that problems exist within the joining companies. Many strategic alliances, although entered into for all the right reasons, do not work. Dissimilar objectives, inability to share risks, and lack of trust lead to an early alliance demise.

(4) Lack of coordination between management teams: Action taken by subordinates that are not congruent with top-level management can prove particularly disruptive, especially in instances where companies remain competitors in spite of their strategic alliance. If it were to happen that one company would go off on its own and do its own marketing and sell its own product while in alliance with another company it would for sure be grounds for the two to break up, and they would most likely end up in a legal battle which could take years to solve.

(**5) Differences in operating procedures and attitudes among partners:** Other problems that can occur between companies in trade alliances are different attitudes among the companies, one company may deliver its good or service behind schedule, or do a bad job producing their goods or service which may lead to distrust among the two companies.

(**6) Relational risk:** Relational risk is concerned with the probability that partner firms lack commitment to the alliance and that their possible opportunistic behaviour could undermine the prospects of an alliance.

(**7) Performance risk:** Performance risk is the probability that an alliance may fail even when partner firms commit themselves fully to the alliance. The sources of performance risk according to a recent study by Das and Teng (1999) include environmental factors, such as government policy changes, war, and economic recession; market factors, such as fierce competition and demand fluctuations; and internal factors, such as a lack of competence in critical areas, or sheer bad luck.

(**8) Strategic alliances might create a future local or even global competitor:** One partner, for example, might be using the alliance to test a market and prepare the launch of a wholly owned subsidiary. By declining to cooperate with others in the area of its core competency, a company can reduce the likelihood of creating a competitor that would threaten its main area of business; likewise, a company can insist on contractual clauses that constrain partners from competing against it in certain products or geographic regions.

Strategic Alliance Checklist

Following checklist captures the key points which organisations should consider before entering into a strategic alliance.

1. *Don't get left behind. Alliances are here to stay. They are a permanent part of the corporate finance and corporate-development tool kit.*
2. *Understand the differences between alliances and Merger and Acquisition. Alliances represent a distinctive form of corporate control.*
3. *Understand when they make sense strategically and when they do not.*
4. *Avoid using alliances as a substitute for merger and acquisition.*
5. *Align the company's alliance strategy with corporate strategy. In particular, know the role of alliances in company's growth strategy.*
6. *Alliances are a way to keep options open in order to participate in growth opportunities.*
7. *Spreading the risks of failure among multiple partners, alliances allow a company to limit its downside exposure.*
8. *Actively manage alliance portfolio. Over time, weed out the value destroyers and nurture the successful partnerships.*
9. *Develop a structured alliance process. Be as systematic in selection of partner and negotiation as in the pursuit of a merger or an acquisition.*
10. *Continuously monitor alliance performance on the basis of explicit criteria for performance.*
11. *Ambiguous governance undermines commitment. Ensure that the governance mechanisms are clear.*
12. *Most alliances don't last forever, so have a clear exit strategy.*
13. *Once active portfolio of alliances is in place, it's important to establish a strong capability in alliance management.*

TRENDS IN STRATEGIC ALLIANCES

Strategic alliances are becoming more and more prominent in the global economy. Peter F. Drucker, who has been called the Father of Management theory, states: "The greatest change in corporate culture, and the way business is being conducted, may be the accelerating growth of relationships based not on ownership, but on partnership".

Indeed, searches on the Internet for strategic alliances produce numerous press releases about companies forming alliances, and also produce several addresses for strategic alliance consulting companies. The number of strategic alliances has almost doubled in the past ten years and is expected to increase even more in the future.

Alliances are being formed across a broad range of sectors, including chemicals and pharmaceuticals, computers and electronic equipment, and financial and business services. A greater number of partnerships are for joint marketing and Research & Development rather than production; this partly reflects the increasing role of service firms in international alliances. In order to achieve global scale in operations, enterprises are choosing international alliances, along with mergers & acquisitions and greenfield investment.

More than other forms of internationalisation, international strategic alliances provide firms with strategic flexibility, enabling them to respond to changing market conditions and the emergence of new competitors. They are prompted by a range of motives, including economising on production and research costs, strengthening market

presence, and accessing intangible assets such as managerial skills and knowledge of markets. In high-technology sectors like pharmaceuticals, research costs and time-lags are driving partnerships.

In telecommunications equipment and other wireless "network" device manufacturing sectors, alliances are directed to developing a new world product or systems standard. In automobiles and many manufacturing industries, achieving economies of scale in production on a global scale may be the prime motive.

In service sectors such as airlines, alliances are aimed at sharing a partner's sales and distribution outlets. In all cases, international strategic alliances are being driven by the economic demands of global markets, the costs of keeping up with fast-changing technologies, and the opportunities provided by government deregulation and liberalisation initiatives.

The recent trends in strategic alliances are different from those of the past in following respects, –

(i) their growing significance as an inter-organisational form for participating firms to enhance competitiveness and to generate innovation-led growth;

(ii) the range, depth and closeness of the interactions among co-operating partners; and

(iii) the effect that such alliances are having upon corporate and overall industrial performance.

CASE STUDIES

Air India and Lufthansa Strategic Alliance

Lufthansa and Air India significantly improved their market leadership positions on India-Europe-USA routes with the Strategic Alliance agreement signed between Lufthansa & Air India. From 1st October 2004, Air India has been a partner of Lufthansa. Within the scope of an extensive agreement covering a far-reaching bilateral cooperation, Wolfgang Mayrhuber, Chairman of the Executive Board of Deutsche Lufthansa AG, and V. Thulasidas, Chairman & Managing Director of Air India, signed a Strategic Alliance agreement in Mumbai. The objective of the partnership was expansion of the offer of flights between Germany and India. All flights between the two countries were operated by the two airlines in code-sharing. New routes were added.

Through the cooperation in the area of frequent flyer programs, customers on flights of both airlines can collect and redeem miles for the respective programmes - Miles & More and Flying Returns. Air India has been accorded the IOSA10 Audit Certificate by IATA11 which puts it in the league of a dozen Airlines conforming to quality standards required for joining Global Alliances.

India - Germany/ Europe and India-USA are very important markets for Air India which it plans to serve over Frankfurt in 10. IOSA (International Civil Aviation Organisation) – A specialized agency of the United Nations whose objective is to develop the principles and techniques of international air navigation. IATA (International Air Transport Association) – A trade association serving airlines, passengers, shippers, travel agents alliance with Lufthansa. In addition to the code-sharing between Germany and India, the code of Air India will also be bookable on Lufthansa connecting flights from Frankfurt to Berlin, Munich, Stuttgart and Düsseldorf to Amsterdam, Geneva, Zurich and Lyon as well as to Washington, Denver, Detroit, Chicago and Los Angeles. This cooperation agreement results from a memorandum of understanding which the two carriers signed on 26th August 2003. In it, cooperation in the area of sales and marketing is also foreseen as well as cooperation in the medium term in other areas, for example, in the area of IT.

Lufthansa which was flying from Frankfurt to Delhi (once daily), Mumbai (once daily), Chennai (once daily) and Bangalore (five times a week) as well as from Munich to Delhi (three times a week.) would fly further six weekly flights between Frankfurt and Mumbai as well as three weekly flights between Frankfurt and Delhi which are operated by Air India and can be booked with a Lufthansa code. Air India served up to 33 destinations from Mumbai and Delhi, including, among others, Frankfurt, Chicago and New York. The fleet of Air India consists of 33 wide bodied aircraft and it had planned to add more to make its Los Angeles & Chicago flights daily. It has

also planned to operate daily services between London and Mumbai & London and Delhi and link Bangalore with Frankfurt four times a week from March 2005. The Lufthansa - Air India pact paves the way for joint development of air services on India-Europe-USA route.

Joint Engineering Design by Ford and ABB

Intent on doing their firm's combined best through achieving synergy, Ford and ABB assembled a joint engineering team and charged members with blending their know-how to find an optimal solution to their cost, cycle time, safety, and other objectives. ABB people shared their knowledge about technologies and processes, while Ford team members contributed their experience with paint plants. The joint team produced a design markedly different from anything from anything that had been done before. It had a smaller footprint, a multistory rather than a one-story structure, a revised system layout, and a far cleaner internal environment – which made a big quality difference in finished cars.

Strategic Alliance by AT&T

AT&T entered in a strategic alliance with a much smaller credit card technology firm to develop a new credit card service. To ensure secrecy – to stay beneath the radar of their main competitors – so that the alliance could maintain a critical lead in the industry, companies established trust-based relationships and no contracts was used for the first several months of this relationship. During this same time, the firms worked collaboratively, sharing information and resources while relying on the character and goodwill of each other to guide the relationship. In examining this relationship, AT&T was more concerned with maximizing the opportunities of the alliance than with minimization of potential opportunism within it.

Strategic Alliance by Nypro

Nypro Inc., the eighth-largest plastics injection molder in the United States, is a global contract manufacturer. The company transformed itself from an undistinguished also-run to an internationally heralded leader in zero-defect production.3 Nypro searched out sophisticated customers, initially targeting cutting-edge manufacturers of health-care products whose needs for product safety demanded far higher specifications than any existing injection process could deliver. Nypro designed new injection process for each customer, sharing insights with the customers' own engineering and marketing teams to solve their specific problems. They worked together: partners in innovation. Nypro situated its new plants next door to its customers and integrated its new process with theirs. As a result, Nypro's customers got more sophisticated products produced at lower costs with a faster cycle time and fewer defects.

LESSON ROUND UP

- A strategic alliance is form of cooperative strategy in which firms combine their resources and capabilities to create competitive advantage. With increasing complexity and dynamism strategic alliances has become integral component of the success story of modern organizations.
- Strategic alliances may mainly take four forms: joint ventures, equity strategic alliance, non-equity strategic alliance and global alliances.
- In a joint venture firms create a new legal entity and own equal shares in it to develop a competitive advantage. In equity alliance firms own different shares of the newly created venture. In non-equity alliance firms cooperate through a contractual relationship.
- Alliances make strategic sense in situations of high uncertainty and in markets with growth opportunities that a company either cannot or does not want to pursue on its own.

- One of the main reasons to engage in an alliance is to share risk and limit the resources a company must commit to the venture in question.
- The commitment of the Senior Management of all companies involved in a strategic alliance is a key factor in the alliance's ultimate success.
- Strategic alliances in the global economy are becoming more prominent & the trends in current alliances are different from those of the past.

SELF TEST QUESTIONS

1. What is 'strategic alliance'? What are the different types of strategic alliances?
2. What are the stages involved in formation of an alliance?
3. What are the advantages of strategic alliances? Enumerate the parameters of a successful alliance.
4. What are the possible reasons for failure of cross cultural alliances?
5. What are the factors to be kept in mind while managing an alliance?

Lesson 12
Logistics Management

LESSON OUTLINE

- Logistics management - Meaning and definition
- Objective of logistics management
- Role of logistics management in an organization
- Stages in logistics management
- Scope of logistics management
- Transportation
- Transport providers
  - common & private carriers
  - freight forwarders
  - Third party logistics (3PL) providers
  - Fourth Party logistics providers (4PL)
- Warehousing
  - Types of warehouses
  - Warehousing (development and regulation) act, 2007
  - Logistics parks
  - Free trade warehousing zone (FTWZ)
  - Central warehousing corporation (CWC)
- Inventory management
- Packaging
- Containerisation
- Control and communication
- Role of Information Technology in logistics
- LESSON ROUND UP
- SELF TEST QUESTIONS

LEARNING OBJECTIVES

Logistics management is an integral factor in the success of any manufacturing companies operations and has direct impact on their bottom line. Logistics management is that part of supply chain management that plans, implements, and controls the efficient, effective forward and reverse flow and storage of goods, services and related information between the point of origin and the point of consumption in order to meet customers' requirements. It is simply the management of the movement of goods.

The overall scope of logistics management typically includes many factors, such as: transportation management, freight and inventory management, materials handling, order fulfillment etc. Many companies look to third party logistic providers (3PL's) for help in managing these activities. An effective logistics management operation increases revenue, improves operating cost structure, reduces overall transportation costs and improves customer service.

Logistics is one of the key areas in the process of international business as the delivery of goods to the buyer is as important as any other activity in business and marketing. Quite often, the most crucial part in International trade is the timely delivery of goods at a reasonable cost by the exporter to the importer. In fact, the prospective buyer may be willing to pay even higher price for timely supplies. The emergence of logistics as an integrative activity, with the movement of raw materials from their sources of supply to the production line and ending with the movement of finished goods to the customer has gained special importance.

In this chapter we will discuss logistics management, its role, objectives and scope. The chapter will also highlight some of the logistics facilities available in India and the emerging trends in India regarding logistics.

"Logistics is the "process of planning, implementing, and controlling the efficient, effective flow and storage of goods, services, and related information from point of origin to point of consumption for the purpose of conforming to customer requirements."

Council of Logistics Management

LOGISTICS MANAGEMENT – MEANING AND DEFINITION

The concept of "Logistics" started many years before Christ and was used by Greek Generals (Leon the Wise, Alexander the Great) in order to describe all the procedures for the army's procurement on food, clothing, ammunition, etc. Alexander the Great was a big fan of the mobility of his troops and he didn't want his troops to stay in one place waiting for supplies from Macedonia. Thus, he tried to resolve the issues of supplies by using supplies from the local resources of his defeated enemies. For many years, logistics were always an issue in war affairs.

Logistics is concerned with getting the products and services where they are needed when they are desired. It is difficult to accomplish any marketing or manufacturing without logistical support. It involves the integration of information, transportation, inventory, warehousing, material handling, and packaging. The operating responsibility of logistics is the geographical repositioning of raw materials, work in process, and finished inventories where required at the lowest cost possible.

The formal definition of the word 'logistics' is: - it is the process of planning, implementing and controlling the efficient, effective flow and storage of goods, services and related information from the point of origin to the point of consumption for the purpose of conforming to customer requirements.

Logistics = Supply + Materials management + Distribution

Logistics is concerned with proper movement of materials from the source of supply to the place of production and movement of finished product from the factory to the customer. Its purpose is to make the product available to the customer at the right place and at the right time. Logistics is also known as 'Physical Distribution Management (PDM)'. It involves efficient management of materials and finished products, their movement, storage, and control. It helps to provide time utility and place utility to customers.

Logistics may be defined as, "the process of strategically managing the movement and storage of materials, parts, and finished inventory from supplier through the firm and on to customers."

Logistics deals with all activities that facilitate product flow from the source of raw materials to the point of final consumption. It comprises transportation, warehousing, order processing, inventory maintenance, product packaging and handling, etc. It recognizes inter connections and inter relationships between these activities and involves their integration into a total system. Logistics comprises physical supply which is concerned with the handling or management of materials, and physical distribution which involves the flow of finished products from the plant to the customers. Physical distribution is also known as Supply Chain Management or Market Logistics.

According to Philip Kotler, "Market Logistics involves planning, implementing and controlling the physical flow of materials and final gods from point of origin to the point of use to meet customer requirements".

Logistics management tries to have the "right product", in the "right quantity", at the "right place", at the "right time", with the "right cost".

Logistics is the management of the flow of resources between the point of origin and the point of consumption in order to meet some requirements. The resources managed in logistics can include physical items, such as food, materials, equipment, liquids, and staff, as well as abstract items, such as time, information, particles, and energy. The logistics of physical items usually involves the integration of information flow, material handling, production, packaging, inventory, transportation, warehousing, and often security. The complexity of logistics can be modelled, analyzed, visualized, and optimized by dedicated simulation software. The minimization of the use of resources is a common motivation.

Logistics is the process of planning, implementing, and controlling the effective and efficient flow of goods and services from the point of origin to the point of consumption.

Logistics can be:

Inbound Logistics	• Inbound logistics is the management of goods and materials are arriving at one's business premises. it is concerned with purchasing and arranging the movement of raw materials, parts etc. from suppliers to manufacturing or assembly plants or warehouses.
Outbound Logistics	• Outbound logistics is related to the storage and movement of the final product from the end of the production line to the end user.

Logistics can also be:

Domestic Logistics	• The management of materials and finished products and their movement, storage, and control is within the boundaries of a particular country.
International Logistics	• The management of materials and finished products and their movement, storage, and control is between the nations.

Difference between domestic and international logistics can be said to arise mainly on account of three major factors:

I. Logistics cost is likely to account for a much higher proportion of the delivered cost of the product in international trade,

II. The mechanics of doing business are much more complex in the context of international (than domestic) logistics, and

III. The political, cultural and institutional factors connected with international logistics are of considerable importance whereas these are not of much consequence in the context of domestic logistics.

OBJECTIVE OF LOGISTICS MANAGEMENT

Logistics Management involves the integration and coordination of various marketing activities so that end markets are served in the most effective manner. The main objectives of Logistics are as follows:

– To reduce costs of physical distribution through optimum number and location of warehouses, more efficient materials handling, better order processing, etc.

– To gain competitive advantage by means of quick and reliable delivery and error free order processing.

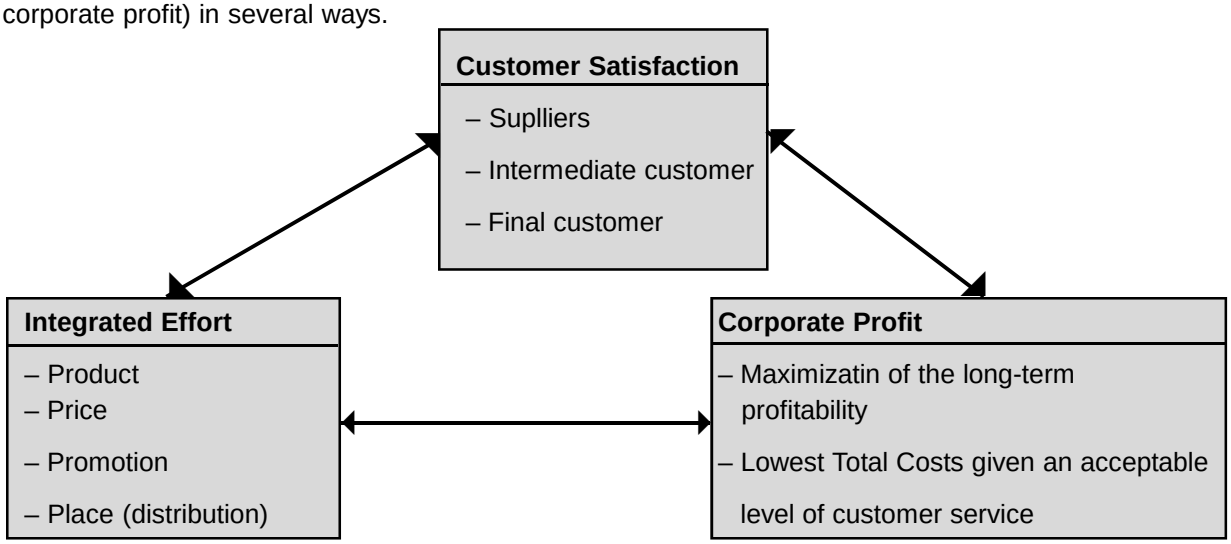
– To improve customer service by minimizing time and efforts in physical distribution.

– To increase sales by ensuring availability of products.

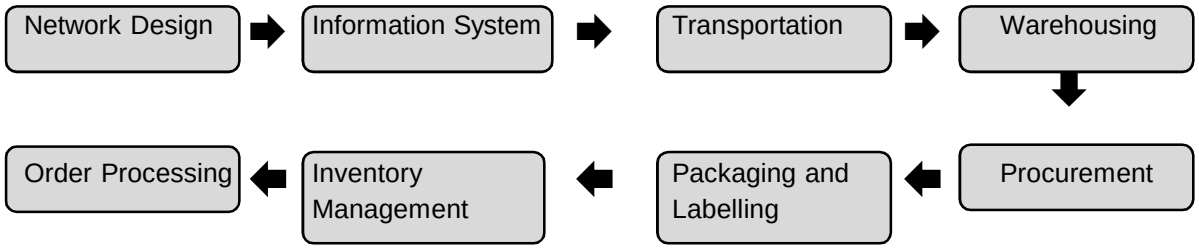
– To develop effective communication system so as to respond quickly to inquiries and complaints of customers.

ROLE OF LOGISTICS MANAGEMENT IN AN ORGANIZATION

Logistics in an organization are considered as a continuation of marketing. Logistics play a critical role in each of the three critical elements of the marketing concept (customer satisfaction, integrated effort/systems approach and corporate profit) in several ways.



STAGES IN LOGISTICS MANAGEMENT



1. ***Network Design*****:** First of all, it is necessary to decide the number and location of facilities needed for logistics operations. Proper design of network and infrastructure improves efficiency of logistics. The facilities in this network are manufacturing plants, materials handling system, distribution system, order processing system, after sale service, etc.
2. **I*nformation*:** In logistics, information is needed to forecast sales and to process customer orders. Sales forecasting helps in inventory management. Correct information is necessary to avoid errors and delays in order possessing.
3. ***Transportation*****:** A cost effective and speedy transportation system improves efficiency of logistics. Roadways, railways, airways and waterways are the different modes of transport. Road transport is suitable for carrying goods of medium bulk and weight over short distances and for point to point service. Rail transport is suitable for carrying heavy goods over long distance. Air transport is suitable for carrying light and valuable goods at a fast speed. Water transport is appropriate for carrying bulky goods of low value.
4. ***Warehousing*****:** Proper storage of goods is necessary to serve customers efficiently, Warehousing decisions are as follows:
   – How many warehouses?

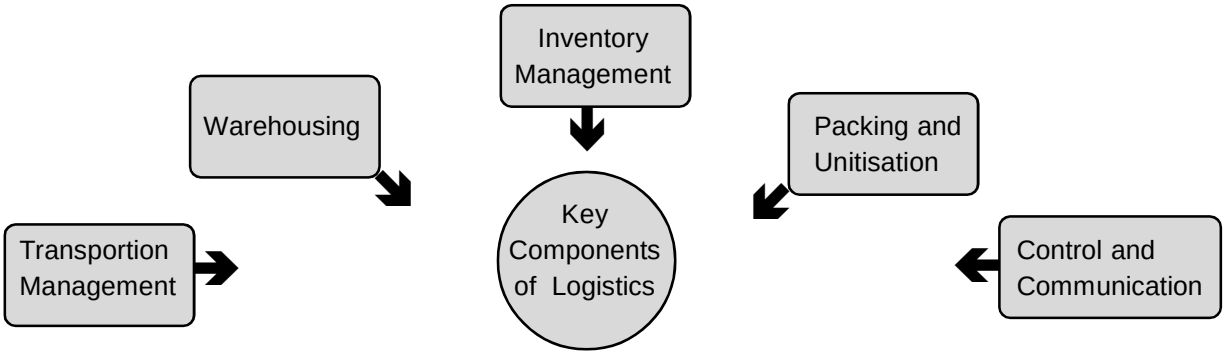
- What type of warehouses?
- Where to locate warehouses?
- What size of warehouses?

5. ***Procurement*:** Acquiring raw materials, semi finished items and a finished product is an important part of logistics. It consists of several activities, e.g., requirement planning, sourcing suppliers, negotiation, order placement, receipt and inspection, quality assurance, handling etc. It provides support to manufacturing and resale operations.
6. ***Packaging and Labelling*:** 'Packaging' involves designing and producing appropriate packages for various products. Effective packaging protects the product, makes product handling convenient and serves as a silent salesman. 'Labelling' refers to putting identification marks on packages. A label provides information about the brand, grade, price, manufacturing date, expiry date, etc. It may be a part of the package or may be attached to the product.
7. ***Inventory Management*:** A business firm maintains inventory to fulfill orders of customers. The amount of inventory will depend upon anticipated demand and time involved in replenishment of inventory. Inventory control involves maintaining inventory at the optimum level so that the costs of carrying inventory and ordering costs are minimized without loss of sales. The nature and quantity of various items to be kept in stock are decided so as to minimize investment in inventory and at the same time avoid interruptions in production process and selling.
8. ***Order Processing*:** The steps involved in executing customer orders are known as order cycle. It begins when customers place an order and ends with dispatch of product to the customer. The order processing system affects customer service significantly. When there are errors and delays in processing of orders, the firm loses customers to its rivals. Therefore, Logistics manager must design and operate a quick accurate and efficient order processing system to retain customers and ensure repeat orders.

SCOPE OF LOGISTICS MANAGEMENT

The scope of logistics management is wider than just optimizing transport costs. Decisions about Logistics have their impact on inventories, on packaging, on material handling and on purchasing and marketing decisions and vice versa. For instance there is no point in producing small but economic batch quantities when the distribution facility dictates that number of these batches should be accumulated before they can be shipped to the customers. Instead of carrying inventory in the plant, one will carry it outside the warehouse. Logistics in a business aim to the following contributions:

- Achieve maximum customer service level
- Ensure high product quality
- Achieve minimum (possible) cost
- Be flexible in the constant market changes



TRANSPORTATION

Transportation provides the flow of materials, products and persons between production facilities, warehouses, distribution centres, terminals and customer locations. Transportation consumes a major proportion of the total logistics costs, so it is very important to plan and implement it intelligently. Transportation Planning generally targets to:

Customer Satisfaction (Quality of Service))	– On-time Delivery – Minimum Delays/Damages/Losses
Productivity Efficiency	– Transit Time Reduction – Lower Variability of Transit Times
Cost Minimization	– Vehicle Acquisition/Fuel consumption minimization – Minimization of Overtimes and excess personnel costs

The goal for any business owner is to minimize transportation costs while also meeting demand for products. Transportation costs generally depend upon the distance between the source and the destination, the means of transportation chosen, and the size and quantity of the product to be shipped. In many cases, there are several sources and many destinations for the same product, which adds a significant level of complexity to the problem of minimizing transportation costs.

Components of Transportation Network

The components of a transportation network can be separated into 3 categories:

Facilities	– Facilities are the fixed component of a transportation network
	– They Include
	  – User-specific Facilities: Warehouses, Terminals, Distribution Centers, Hubs, Docks, etc.
	  – Common Facilities: Roadways, Rail tracks, Waterways

Equipment	– Consists of the various parts of a transportation network. Usually equipment belongs and is maintained by the shippers or the carriers and includes: – Containers, Trailers, Vehicles (tracks, scooters), Rail (Cars, locomotives), aircrafts, vessels
People	– People that are involved in transportation-related or transportation supportive functions are one of the crucial components of transportation networks. – Related working positions are Operating Personnel (Drivers, Pilots, etc.), Supportive Personnel (Maintenance, Loading, Unloading, etc.) and Managerial Personnel (Logistics Directors, Dispatchers, Administration)

Types of transport modes

Rail, road, air, water and pipeline are the five modes of transportation used by logistics management to transport material from one place to another. Each of these modes has some advantages and some limitations. A logistics expert needs to understand these and based on priorities, product type, lead time, etc. decide the appropriate mode of transportation.

1. Air

This mode of transportation is usually used for the delivery of goods from distant suppliers, usually the ones that are not connected by any other mode of transportation. This mode of transport is useful to delivery products with short lead times, fragile goods and products that are not bulky. Also the products that are in high demand and in short supply are also at times air freighted in order to meet customer demands. The bulk/value ratio will be a determining factor.

Advantages :

(i) Fast delivery, usually between 24 and 48 hours

(ii) Faster fulfillment of customer orders

(iii) Ideal for perishable and other products with short life

(iv) Reduced lead time on supplier

(v) Lesser inventory

(vi) Improved service levels

Disadvantages :

(i) Flight delay and/or cancellations especially when direct connections are not available.

(ii) Customs and excise formalities leading to delays.

(iii) High cost.

(iv) Suppliers/customers are not always located near a rail freight depot and delivery to/from the depot can be costly and time consuming.

2. Sea

Sea transportation is used by businesses for the delivery of goods from distant suppliers. Most sea transportation is conducted in containers which vary in size. Goods can be grouped into a container (LCL) or fill a container (FCL). Sea tankers are used for bulk shipments of loose goods such s oil, grain and coal.

Advantages :

(i) Ideal for transporting heavy and bulky goods

(ii) Suitable for products with long lead times.

Disadvantages :

(i) Longer lead/delivery times.

(ii) Problems arising due to bad weather.

(iii) Difficult to monitor exact location of goods in transit.

(iv) Customs and excise restrictions.

(v) High cost.

(vi) Suppliers/customers are not always located near a rail freight depot and delivery to/from the depot can be costly and time consuming.

3. Rail

Rail transportation is popular with businesses for the delivery of a wide range of goods including coal, steel and other heavy goods.

Advantages :

(i) Faster and quicker.

(ii) Ability to carry high capacity.

(iii) Cost effective.

(iv) Safe mode of transport.

(v) Reliable.

Disadvantages :

(i) Subject to unforeseen delays and/or accidents.

(ii) Completely governed by timetable and schedule of railways.

(iii) Suppliers/customers are not always located near a rail freight depot and delivery to/from the depot can be costly and time consuming.

4. Road

A very popular mode of transport used by suppliers and businesses to deliver orders. Many transport companies provide scheduled delivery days and next day delivery services, depending upon your needs. Goods can be packed/grouped in box vans or in containers which are also used for sea transportation.

Advantages :

(i) Cost effective.

(ii) Fast delivery

(iii) Ideal for any short distances

(iv) Refrigerated vans can be easily used for transporting perishables.

(v) Easy to monitor location of goods.

(vi) Mass movement of goods

(vii) Point-to-point service.

(viii) Easy to communicate with driver. Usually companies ask the driver to call the company every couple of hours.

Disadvantages :

(i) Delays due to traffic jams, octroi snarls, etc.

(ii) Problems due to vehicle breakdown, accidents, etc.

(iii) Goods susceptible to damage and losing quality.

(iv) Heavy dependability on weather.

5. Pipeline

Advantages

(i) Mass movement of liquids and gases

(ii) Low operating costs.

Disadvantages

(i) Limited applicability

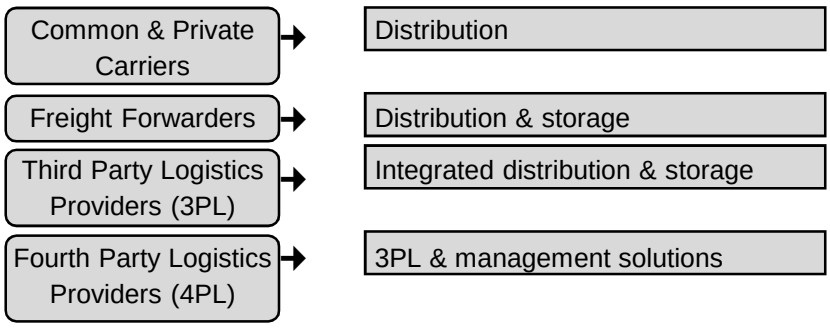
(ii) Not widespread.

Type of Transport – Summary

Air	– Although air transportation is considered as expensive, it offers long-distance transportation in short time periods. – Air transportation depends heavily on weather conditions and delays in schedule may occur.
Sea	– Sea Transportation offers the ability to carry large quantities of commodities {in 000' tones} using specialized cargo ships. – Sea Transportations offers low flexibility in determining routes and schedules. – Depends on weather conditions
Rail	– Rail transportation is considered as a slow transport mode – Low cost materials and raw materials are usually transferred. – Weather conditions do not influence rail operations. – Many stops in local areas can be made in order to load/unload commodities.
Road	– Offers lower capacity in comparison with rail transportation – Advantage of road transportation is the ability to offer door-to-door services and the existence of many different and specialized vehicles. – Weather conditions do not influence road operations to a great extent.
Pipeline	– Used to transport Liquids and Gases (i.e. Oil, Natural Gas) – Although transportation is slow (3-4 miles per hour), the ability to operate 24 hours a day makes it an efficient transportation mode of these product types. – As in rail transportation, offers a specific network with specific stops, intersections, etc. – Weather conditions do not influence pipeline operations and limited technical problems may occur.

TRANSPORT PROVIDES

Warehousing and Transportation of products / commodities consist of one of the core procedures in business operations. These procedures can be performed by own resources or by external partners. Each company selects transport providers based on their needs and the types of services required.



(1) Common & Private Carriers

A common carrier is a business that transports people and/ or goods, offers its services to the general public under license or authority provided by a regulatory body. Common carriers typically transport persons or goods according to defined and published routes, time schedules and rate tables upon the approval of regulators. Public airlines, railroads, bus lines, cruise ships, motor carriers (i.e., trucking companies) and other freight companies generally operate as common carriers. Any person who undertakes to transport goods is simply referred to as a carrier. In contrast, private carriers are not licensed to offer a service to the public.

Private carriers generally provide transport on an irregular or ad hoc basis for their owners. It should be mentioned that the carrier refers only to the person (legal or physical) that enters into a contract of carriage with the shipper. The carrier does not necessarily have to own or even be in the possession of a means of transport. Unless otherwise agreed upon in the contract, the carrier may use whatever means of transport approved in its operating authority, as long as it is the most favourable from the cargo interests' point of view. The carriers' duty is to get the goods to the agreed destination within the agreed time or within reasonable time.

(2) Freight Forwarders

Freight Forwarders are not the classic common carriers. Their business is to:

- Hire "transport space" from transportation means (carriers, ships, etc.)
- Group and integrate loads and shipments

The advantages of the existence of freight forwarders and their provided services can be summarized in the following:

- They succeed in better transport means' capacity utilization (due to consolidation of shipments)
- Consolidation of shipments and the handling of larger integrated loads/ shipments leads to efficient material handling (loading, unloading, trans-shipment, etc.)
- Due to the consolidation and the trans-shipment of larger shipments, freight forwarders succeed in lower- transport prices with the transport means' operators, leading to minimized cost in comparison with sending smaller shipments by each shipper.

(3) Third Party Logistics (3PL) Providers

Third-party logistics (3PL) refers to outsourcing transportation, warehousing and other logistics related activities to a 3PL service provider that were originally performed in-house. Third-party logistics (3PL) or logistics outsourcing is gaining importance as more and more corporations across the world, unable to manage their complex supply chains, are outsourcing logistics activities to the 3PL or logistics service providers. By outsourcing logistics activities, corporations are able to not only concentrate on their core business operations, but also achieve cost-efficiency and improve delivery performance and customer satisfaction. The concept of a single professional logistics service provider managing the entire logistics functions of a company, had originated in the developed economies of Europe and America, to relieve industries from huge logistics costs apart from the hassles of dealing with multiple in-coherent logistics service providers. It proved to be immensely successful in improving logistics efficiency of majority of industries and quickly gained popularity, spreading across the globe. In the process, several professional logistics service providers offering that kind of services have emerged to be leading 3PL providers with operations in multiple continents.

In the initial stages, 3PL providers offered only basic logistics services such as warehousing and transportation. But with growing logistics needs of organizations to remain competitive in globalized economies, 3PL providers have evolved to offer several other value added services ranging from packaging to supply chain planning. 3PL companies provide a wide variety of services, apart from simple distribution and storage procedures.

Advantages of 3PL providers

- Investments to facilities like warehouses, trans-shipment centers or equipment vehicles, are not required.
- Costs / expenses are known in advance in detail and based on the transported volumes and distances.
- It provides economies of Scale as it is cheaper for small manufacturers and shippers in contrast to maintain own facilities and fleets.
- It is easier to change the operational logistics model, in order to succeed in more efficient logistics services, than re-engineer the company's own logistics services (if there are already fixed facilities and resources)
- Companies can focus to their core business operations (sales, marketing, etc.)
- Companies can gain immediate access to intelligent IT & Telematics infrastructure (without the additional cost of investment)
- Offers great flexibility in market penetration (due to the wide distribution network of a 3PL company)
- 3PL companies offer a wide variety of vehicles that can undertake commodities with specialized characteristics and even use multiple-compartment vehicles that can transport different products simultaneously (i.e. frozen goods with simple product compartments in a vehicle).

Disadvantages of 3PL providers

- Using 3PL providers may lead to lose control of the distribution and storage procedures of the products.
- 3PL providers have a physical advantage in comparison to the shippers and the shipper may start to depend on specific 3PL providers.
- Shippers cannot gain expertise and experience in distribution and storage operations and processes (and it becomes difficult to re-adapt a non-3PL distribution and storage model).
- Service provision issues may arise: (1) the company's sales and deliveries to customers may not be aligned and in-time and (2) there is no direct contact with customers.
- Trust issues may arise as 3PL companies serve different competitive shippers.

Factors for the growth of 3PL providers

- Due to globalization, corporations across the world are increasingly sourcing, manufacturing and distributing on a global scale, which makes their supply chains very complex for them to manage. Hence they have to outsource their logistics activities to experienced 3PL providers, who have global operations.
- Logistics outsourcing is used to complement the logistics activities the corporations do not have competency in, and also to increase the geographic reach. When a corporation expands business overseas, it may not be conversant with the customs duties, tax structures, rules and regulations, import/ export policies of the government, and culture of the foreign country. A 3PL provider, who has long been operating in that country, will be better able to carry out the logistics operations.
- Logistics outsourcing may also reduce costs as the 3PL providers can get the advantage of the economies of scale, which is otherwise not available to the corporations.
- By outsourcing logistics, corporations can reduce their asset base, and deploy the capital released for other productive usage.
- Logistics outsourcing improves cycle time and delivery performance, thereby increasing customer satisfaction.

- Since the 3PL providers are now offering a number of value-added services such as customs clearance, freight forwarding, import/export management, distribution, after sales support, reverse logistics and so on, corporations can outsource all these activities, and concentrate on their core business operations.
- Due to an incredible growth in electronic retailing since the late 1990's, many firms around the world with virtually no distribution systems rely heavily on the 3PL providers for delivery of the merchandise at the customer's doorstep. This has resulted in a significant growth in the order fulfillment sector of the 3PL service industry.

3PL INDUSTRY IN INDIA

3PL industry's origin in India can be traced back to mid 1990s. The industry was pioneered by global logistics majors as a part of extending these services to the Indian subsidiaries of multinational companies in automobile, electronics and FMCG sectors. Indian subsidiaries of multinational companies in these sectors took cue from their parent companies and began to outsource a share of their logistics functions to these specialist service providers. Though insignificant in the first few years, Indian 3PL industry is experiencing a rapid growth after year 2000. The Indian 3PL industry can be divided into three distinct tiers - National Major 3PL companies with nationwide presence, Regional 3PL companies with strong presence in one or two regions, and Small Remote 3PL companies.

There are some operational and regulatory roadblocks to the growth of the 3PL market in India. The major problems are outlined below.

- The Indian firms are still wary of outsourcing their logistics activities due to lack of trust and awareness. The 3PL activity is less than 10% of the total logistics operations in India, whereas the corresponding figures for the U.S, Europe and Japan are 57%, 40% and 80% respectively.
- The poor infrastructure of India acts as a deterrent for attracting investments for the logistics sector. The national highways constitute 1.4% of the total road network, but carry 40% of the total freight movement by roadways. Owing to a bad condition of roads and inadequate communications infrastructure, 3PL providers would not be able to provide quality service to their clients, and hence would not be able to attract business from the Indian firms. The unwillingness of the Indian firms to outsource logistics operations due to lack of trust and awareness and the unwillingness of the 3PL providers to bring in more investments due to a poor infrastructure constitute a vicious cycle and act as a major roadblock to the growth of the 3PL market in India.
- The logistics firms offer limited services. In order to attract more business, they have to offer more value-added services, namely packaging and labeling, order management, order fulfillment, distribution, customer support, fleet management, freight consolidation, reverse logistics and logistics consulting.
- The 3PL providers in India are caught on the wrong foot because of the differential sales tax policy of the Indian Government. Currently, the 3PL providers have to set up warehousing facilities in a number of states to avoid double taxation, thus losing the advantage of the economies of scale.

Despite the problems mentioned above, the 3PL market in India is expected to grow. Some of the large Indian corporates such as Reliance, Tata, Mahindra and Mahindra, TVS Group and Essar Shipping have already forayed into the logistics business. Initially these corporates formed divisions to handle internal logistics, but sensing the potential of the market, they have started offering logistics solutions to other Indian corporates and have already turned these logistics divisions into profit centres. Some large express cargo and courier companies such as Transport Corporation of India Ltd. (TCIL), Gati, Safexpress and Blue Dart have also started offering 3PL services. Transport Corporation of India is one of the India's largest private deemed integrated supply chain and logistics solutions provider and a pioneer in the sphere of cargo transportation in India. Leveraging on its extensive infrastructure, strong foundation and skilled manpower, TCI offers seamless multimodal transportation solutions.

FOURTH PARTY LOGISTICS PROVIDERS (4PL)

4PL is new concept is supply chain outsourcing. It is the next level in logistics out-sourcing and is considered as a path to achieve more than the one time operating cost reductions and asset transfers of a traditional outsourcing arrangement. A 4PL forms an alliance between best-of-breed third party service providers, technology providers and management consultants and this helps them provide unique and comprehensive solutions that go beyond the traditional domain of logistics outsourcing.

A fourth party logistics provider is a supply chain integrator that assembles and manages the resources, capabilities and technology of its own organization with those of complementary service providers to deliver a comprehensive supply chain solution. Thus a 4PL solution leverages the combined capabilities of both management consulting and third party logistics providers.

While the TPL providers have focused on operational issues such as implementation and execution, a 4PL brings in managerial inputs to the table, thereby providing the complete supply chain synchronization and collaborative advantages.

To build up this strength, many third party service providers are going for collaborations mainly with consultancies and technology providers. Now corporations are outsourcing their entire set of the supply chain process from a single organization which will assess, design, make and run integrated comprehensive supply chain solutions.

Stages of Fourth Party Logistics Solutions

1. Reinvention : At the highest level of fourth party logistics, is reinvention. Reinvention takes advantage of the traditional supply chain management consulting skills, aligns business strategy with supply chain strategy and is facilitated by technology that integrates and optimizes operations both within and across participating supply chains.

2. Transformation: The next level is transformation which focuses on improving supply chain functions that are internal to the organization. This includes sales and operation planning, distribution management, procurement strategy and customer support. Technological leadership an excellence is leveraged with strategic thought, process redesign and organization change management to improve and integrate these supply chain activities by bringing about the best breed solution. The main thrust of a 4PL is bringing the best in breed applications.

3. Implementation: How to efficiently use and implement solutions provided by best in breed consultants to leverage the advantages of supply chain management is the next level. This includes business process realignment, technology and system integration across the client organization and service providers and transition of the operators to the delivery team.

4. Execution: The fourth party logistics provider takes the operational responsibility for multiple supply chain functions and processes. It covers transportation management, warehouse operations, manufacturing, procurement, supply chain, information technology, demand forecasting, network management, customer service management, inventory management and administration.

In summary, the fourth party logistics responds effectively to the broad complicated needs of today's organizations by delivering a comprehensive supply chain solution. This solution is focused on all elements of SCM, continuously updated and optimized technology and is tailored to specific client needs. Information Technology can greatly influence and enhance the effectiveness of fourth party logistics. Implementing systems at levels of ERP, DSS, etc. at both transactional and functional levels can allow an organization to redirect the product flow, if desired, and forecast the volumes. It also allows the user to track performance accountability at all levels within the supply chain line while monitoring continuous performance opportunities.

Cost effectiveness of Fourth Party Logistics

1. Revenue growth by enhanced product quality, product availability, and improved customer service, all facilitated by the application of leading technology.

2. Operating cost reduction can be achieved through operational efficiencies, process enhancements and procurements. Savings will be achieved by compete outsourcing of supply chain functions and not just selected components.

3. Fixed capital reductions will result from capital asset transfer and enhanced asset utilization. The fourth party logistics organization will own physical assets through freeing up the client organization to invest in core competencies.

WAREHOUSING

The words 'warehouse' and 'godown' are synonymous. Warehouse means any building structure or other protected enclosure which is used or may be used for the purpose of storing goods on behalf of the depositors but does not include cloak rooms attached to hotels, railway stations, the premises of other public carriers and the like.

A warehouse is a commercial building for storage of goods. Warehouses are used by manufacturers, importers, exporters, wholesalers, transport businesses, customs, etc. They are usually large plain buildings in industrial areas of cities and towns and villages. They usually have loading docks to load and unload goods from trucks. Sometimes warehouses are designed for the loading and unloading of goods directly from railways, airports, or seaports. They often have cranes and forklifts for moving goods, which are usually placed on ISO standard pallets loaded into pallet racks. Stored goods can include any raw materials, packing materials, spare parts, components, or finished goods associated with agriculture, manufacturing and production.

Historically warehouses were a dominant part of the urban landscape used from the start of the Industrial Revolution through the 19th century and into the twentieth century: the building remained when their original usage had changed.

Types of warehouses

- Public warehouses
- Private warehouses
- Bonded warehouses
- Government warehouses
- Co-operative warehouses
- Container freight stations (CFS)/inland container depots (ICDs)
- Cold storage

(1) *Public warehouses*: Warehouses, licensed by the government to private entities, individual or cooperative societies to store goods of the general public are called public warehouses. Usually, these warehouses are set up at transportation points of railways, highways and waterways, providing the facilities of receipt, dispatch, loading and unloading of goods. They are rented out against a certain fee. The government also regulates the functions and operations of these warehouses used mostly by manufacturers, wholesalers, exporters, importers, government agencies, etc. They are economical and easily available storage facilities for small manufacturers and traders too. Some warehouses provide facilities for the inspection of goods and also permit packaging and grading. The public warehousing receipts serve as good collateral securities for borrowings.

(2) *Private warehouses*: These warehouses are owned by private entities or individuals and are used exclusively for the goods owned, imported by or on behalf of the licensee. The warehouses are usually constructed at strategic locations to cater various manufacturing, business and service units. They are flexible enough to be customised in terms of storage and placement, according to the nature of the products.

(3) *Bonded warehouses*: The concept of bonded warehouses was developed in order to facilitate the deferred payment of customs duty by entrepreneurs, exporters and importers, to enable them to carry out their operations with least investment. These warehouses are used to store imported goods under an undertaking or 'bond', which does not allow the release of goods until the custom duties are paid. These are generally owned, managed and controlled by both government and private parties and are established near ports. Government and private parties together manage bonded warehouses. The Central Warehousing Corporation operates 75 custom-bonded warehouses with a total capacity of nearly 0.5 million MTs located at Ahmedabad, Bangalore, Bhopal, Chandigarh, Chennai, Delhi, Hyderabad, Jaipur, J N Port, Kolkata, Kochi, Lucknow and Mumbai.

(4) *Government warehouses*: These warehouses are owned, managed and controlled by central or state governments, public corporations or local authorities. These warehouses can be used by both government and private organisations. CWC, SWC and FCI are examples of agencies maintaining government warehouses.

(5) *Co-operative warehouses*: These warehouses are owned, managed and controlled by co-operative societies. They provide their members with warehousing facilities at cheaper rates.

(6) *Container Freight Stations (CFS)/Inland Container Depots (ICDs)*: CFSs/ICDs are custom-bonded facility with public authority status for the handling and storage for containers. These depots are equipped with warehousing space, adequate handling equipment and IT infrastructure. Services of CFS/ICDs include the following:

- Loading/unloading
- Receipt/dispatch of goods
- Transit operations by road/rail to and from the port
- Stuffing/de-stuffing of containers
- Customs clearance
- Consolidation and desegregation of Less than Container Load (LCL) cargo
- Temporary storage of cargo and containers
- Repair and maintenance of containers
- Refrigerated warehousing
- Hub-and-spoke services

CFS is an off-dock facility located near the service port. ICD, on the other hand is located in the hinterland. CFSs/ICDs act as consolidation points, transit storage locations and ease the compliance procedure with local customs, reduce damage/pilferage, optimise container utilisation and reduce transport/ inventory cost.

(7) *Cold storage*: A cold storage is a temperature-controlled storage space and caters to industries such as agriculture, horticulture, fisheries and aquaculture, dairy and processed food. Cold storage preserves agricultural products. Refrigerated storage helps in eliminating sprouting, rotting and insect damage. Edible products are generally not stored for more than one year. Several perishable products require a storage temperature as low as -25°C.

Cold storage helps stabilize market prices and evenly distribute goods both on demand basis and time basis. The farmers get the opportunity of producing cash crops to get remunerative prices. The consumers get the supply of perishable commodities with lower fluctuation of prices.

The temperature necessary for preservation depends on the storage time required and the type of product. In general, there are three groups of products, foods that are alive (e.g. fruits and vegetables), foods that are no longer alive and have been processed in some form (e.g. meat and fish products), and commodities that benefit from storage at controlled temperature (e.g. beer, tobacco).

Location is a very critical aspect for the success of cold storage. It should be in close proximity of a growing area as well as a market, be easily accessible for heavy vehicles, and have uninterrupted power supply. The key activities involved in cold storages are as follows:

- Aggregation
- Sorting
- Pre-cooling
- Packaging from farms to manufacturers

Role of IT in warehousing

Today the role of technology has transformed from being an enabler of productivity and quality through process automation and quality control to a more strategic role as a key influencer of competitive advantage. The last decade of the 20th century has witnessed rapid technological advances, especially in IT. Increase in IT adoption and knowledge infrastructure can provide a boost to the growth and maturity of warehousing players in India. IT has today presented enterprises with possibilities of delivering substantial operating savings while at the same time improving the quality of order fulfillment. India's warehousing technology market in India is growing steadily, with the upswing in demand from the thriving logistics, retail and manufacturing sectors, as well as government promotion. As the booming manufacturing and retail sectors are the main users of these technologies, sustained demand from these areas is ensured. For instance, Wal-Mart has made it mandatory for its suppliers to deploy Radio Frequency Identification ('RFID'). The growth of India as a major sourcing nation for the world's leading retailers is also ramping up demand. Until recently, the logistics industry was highly unorganised, comprising predominantly medium and small-sized Layered Service Providers ('LSPs'). However, the trend is changing with the increase in the number of organised LSPs and improvement in the services offered by them through 3PLs and 4PLs. To obtain the cutting edge in the market, logistics and dedicated warehousing companies are adopting these technologies to improve warehousing and supply chain management. This enables them to achieve maximum warehousing efficiency.

Advantages of IT warehousing

IT adoption has the following advantages that can help warehousing players increase their competitiveness:

- ***Reduced labour costs*:** Automated storage and orderpicking systems can reduce the need for labour and wheeled machinery in the warehouses. In automated goods to person order-picking systems, the right goods are brought automatically to the right person at the right time. This eliminates the need to walk, increasing the productivity of slower-moving Stock Keeping Units ('SKUs') nearly 10 times from traditional zone-picking or pick-to-pallet approaches. Higher productivity automated systems also reduce the number of operators required for storage, picking, packing, etc.
- ***Improved space efficiency*:** By making maximum use of headroom and minimising aisle widths, automated storage systems for pallets, tote-bins and cartons, we can reduce footprint requirements for stock storage and with it land and storage costs.
- ***Improved ergonomics and safety*:** Automated storage systems reduce the need for forklift trucks and eliminate the need to have pallet movements interleaved with other tasks such as order-picking. Automated goods to person palletising stations provide for sliding rather than lifting of cases. Also, ergonomic pick-from-tote stations for small and split-case items minimise bending and twisting, reducing injuries, complaints and lost time.

- ***Flexibility to different order profiles*:** Automated order-picking systems are equally productive for small as well as large orders and the productivity is independent of the number of SKUs as against the manual systems, where more SKUs and smaller orders mean greater walking distances which reduce productivity.
- ***Higher customer satisfaction*:** Automated order-picking systems allow for greater flexibility with respect to how and when an order is assembled and the order to be picked up at any time, improving response times and increasing fulfillment consistency and quality. All this contributes to higher customer satisfaction.
- ***Quick response and access to information*:** Automation of warehouses through warehouse management systems helps eliminate paperwork and costly shipping errors by helping access the information quickly and efficiently.
- ***Track and trace*:** Warehouse management systems can track inventory throughout the warehouse and the movement of the product from one location to the next.
- ***Standardised procedures*:** Use of warehouse management systems ensures standardisation of processes and procedures such as set acceptance standards for product receipt, monitoring vendor performance, managing customer inventory, expediting orders more efficiently, etc.

Warehouse Management Systems

Warehouse Management Systems (WMS) is one of the most significant technologies used for logistics which enables efficient management of material flow, proper tracking of the movement of goods and on-time delivery of goods to customers. WMS is a system to manage the segment of an enterprise's logistics function responsible for the storage and handling of inventories beginning with supplier receipt and ending at the point of consumption. It is a software application that supports the day-to-day operations in a warehouse, by enabling centralised management of tasks such as tracking inventory levels and stock locations. Its primary objective is to manage a warehouse's resources, including space, labour, equipment, tasks and flow of material.

Today, a complete warehouse management system incorporates picking, inventory control, label-printing, return material authorisation (RMA), receiving and automatic data collection (ADC), wave/batch/zone picking, task-interleaving, integration with automated material-handling equipment, cycle-counting, cross-docking, pick-to-carton/pick-to-light, yard management, transport management, labour management and voice-picking, multiple inventory ownership, billing and invoicing and voice-directed distribution and much more.

There are multiple forms of WMS solutions available in market used by LSPs. The need for WMS is completely dependent on the complexity (in terms of size and volume) of warehousing operations and throughput efficiency (in terms of operational productivity):

- For service providers with small godowns in cities or towns storing small amounts of inventory catering to local markets like local distributors and suppliers and whose operations are simple with limited volumes, traditional ways of managing operations and tracking inventory is still the best bet.
- For service providers operating at a regional level who have significantly large operations with considerable volumes like regional distributors, small logistics firms managing inventory for their customers, or replenishment locations for retailers, mini WMS solutions are available that are good in managing inbound and outbound operations and can also manage and track inventory levels. Organisations using various ERPs can also extend their ERP systems and use a WMS module that will help resolve integration challenges. Such solutions can be customised and are also easy on the pocket.
- For service providers running large warehouses and 3PL companies having multiple customers and facilities spread across the nations. These organizations have multitude transactions and inventory movements within and outside their network. For these organizations , WMS systems can manage

inbound, outbound, value-added service, work order management, quality checks, picking, packing, shipping are needed. RFID integration, global inventory view, intelligent analytics, ERP integration etc.

Typical features needed are:

- Timely order fulfillment
- Economical management of resources
- User-friendly features
  - Ability to cater to typical Indian requirements including legal and statutary requirements taxations, road permits, etc.
  - Rich functionalities as provided by Best-of-Breed (BoB) solutions proven in thousands of sites across the globe having the ability to cater to growing volumes
  - Ability to manage and operate each and every movement in a warehouse
  - Shorter implementation cycles
  - Ability to track, trace and centrally manage inventory stocked in all facilities, channels, regions and networks
  - An intelligent analytics and dashboard to manage KPIs
  - Ease of integration with ERPs like SAP and Oracle
  - Competitive pricing

Other technology interventions

- WMS solutions can be standalone, like those supplied by RedPrairie, Infor, Manhattan Associates or can be part of an ERP application as in the case with warehouse management solutions from SAP, Oracle and other IT solution providers in the domain. Several ERP-based WMS are being used in India for warehouses attached to factories.
- Heavily automated facilities are using a warehouse control system (WCS) that controls conveyor belts, carousels, and other materials-handling systems.
- Retail-warehouse management systems are implementing automatic data detain and identification technology integrated with mobility solutions such as mobile computers, GPS, SMS gateway linking barcode scanners and RFID. These can professionally supervise product flow all through the warehouse.
- The warehousing sector in India is also using voice-based solutions that provide the 'process logic' that directs a warehouse employee to perform functions with accuracy. These solutions free the workers' hands and eyes allowing them to completely focus on their work and communicate with the WMS system using the most natural form of human communication, which is voice.

Barriers to IT adoption in warehousing

Although the prospects for the warehousing technology market look upbeat, there are some challenges preventing forward momentum. The sector is generally perceived to be reluctant in investing in IT. Several factors like the unorganised and fragmented nature of the sector, lack of regulatory compulsions and the view of the players of IT as an expense rather than an investment are said to have contributed to the low penetration of IT in this sector. Some of the factors that act as barriers to IT adoption in the warehousing sector have been detailed below:

- ***Absence of affordable solutions*:** Technologies such as WMS and RFID are significantly expensive, making them unaffordable for a majority of LSPs, warehousing players and end-users. The price-sensitive

nature of the Indian consumers prevents them from opting for such technologies. This has deterred the growth of the warehousing technology market.

- ***Cost:*** Most warehousing players are cautious about investing in an expensive full-scale WMS. They find it easier and quicker to employ more people. Larger acceptance of low-cost or in-house applications has also hindered the acceptance of sophisticated WMS systems. Lack of long-term planning and small warehouse sizes also do not justify the cost of WMS implementation.
- ***IT budget*****:** Most warehousing firms do not have a formal IT budgeting process and hence don't plan for IT investments.
- ***Network infrastructure issues*****:** Reliability and affordability are key network infrastructure concerns for a majority of warehousing players, especially those that have warehouses in remote areas.
- ***Awareness of IT benefits*****:** The management in most warehousing firms are small entrepreneurs who do not have a good understanding of IT and its benefits. The skilled resources in the warehousing sector have very limited exposure to IT thereby creating an understanding gap on the value proposition of IT utility vis-a-vis IT investments. Though there is no dearth of good WMS solutions in the market, there is a dearth of management keen on implementing WMS at their warehouse, keeping long-terms benefits in mind.
- ***Training issues*****:** Very few warehousing sector employees undergo IT training during the course of their employment.

WAREHOUSING IN INDIA

The warehousing landscape in India is witnessing multiple interesting trends, including increasing opportunities across many user segments, emergence of attractive tier-2 cities as warehousing locations and several key buying preferences of customers.

As the Indian transportation and logistics market witnesses new heights, there has been increasing buzz around technology adoption, network optimization, multimodal transportation and improving warehousing. The latter in particular has been evolving rapidly from traditional 'godowns' to modern facilities. Driven by growth in production and consumption, organized retail, logistics outsourcing, modern assets and the likely rollout of Goods and Service Tax (GST), the demand for warehousing space is estimated to grow from 391 mn sq. ft. in 2010 to 476 mn sq. ft. in 2013, growing at 6.8 percent CAGR during this period.

Warehouse (Development and Regulation) Act, 2007

Despite the importance of agriculture in the economy, no adequate steps have been taken to protect the agricultural produce of the country. The introduction of the Warehousing Development and Regulatory Authority (WDRA) will make provisions for the development and regulation of warehouses. The government launched the Negotiable Warehouse Receipts (NWR) system to help farmers gain access to loans from banks and allow the transfer of ownership of that commodity stored in a warehouse without having to deliver the physical commodity. NWRs are negotiable under the Warehouse (Development and Regulation) Act, 2007 and are regulated by the WDRA. These receipts are expected to improve the borrowing capacity of farmers as well as the quality of the bank's lending services in the agriculture sector, increase liquidity in rural areas as well as encourage better price risk management in agriculture commodities. The provisions of WDRA also lead to increased efficiencies in the lending portfolios of banks, as well as further enhance the interests of lending institutions in ensuring credit with reference to goods in warehouses. The NWRs will enable the transfer of ownership of agricultural commodities stored in warehouses without having to deliver physical commodities to the financial institution. This in turn is expected to reduce the wastage/pilferage of goods during their transit from the place of production to the custody of banks/ financial institutions. The implementation of warehousing receipts under the supervision of WDRA is expected to ensure the smooth functioning of the system to foster the growth of warehousing in India.

Logistics park

A logistics park is a stipulated area that facilitates domestic and foreign trade by providing services such as warehousing, cold storage, multi-modal transport facility, CFS, ICDs, etc. Logistics parks facilitate loading and unloading of cargo for distribution, redistribution, and packaging and repackaging. They are developed in the vicinity of emerging industrial hubs such as Mumbai, Chennai, Hyderabad, Bangalore and NCR. Speciality logistics parks are being constructed for industries such as automobile, pharmaceuticals, agriculture, electronic hardware and aero industry. These parks are being connected through well-laid rail links and multi-modal transport facilities. Logistics parks are similar to FTWZs but also cater to the domestic market.

Free Trade Warehousing Zones (FTWZ)

Free Trade Warehousing Zones (FTWZ) were established by the government to develop infrastructure to facilitate import and export of goods and services with the freedom to carry out trade transactions in the free currency. These zones are established close to seaports, airports or dry ports, to be easily accessed by road or rail. According to the Special Economic Zones Act 2005, a FTWZ is a special category of Special Economic Zone (SEZ) and is governed by the provisions of the SEC Act and the Rules. FTWZ are foreign territories to carry on business and are envisaged to be integrated zones to be used as international trading hubs. The minimum area of development under FTWZ is 0.1 million sqm, with 100% FDI approved.

Some of the features of FTWZs are as follows:

- Customised categorised warehouses for industries such as chemicals, food, electronics, oil, etc
- Sophisticated freezer/cooler facilities
- Break bulk, containerised, and dry cargo storage facilities
- Controlled humidity warehouses
- Enhanced transportation facilities
- World-class information system for cargo tracking, etc.
- Office space
- Support facilities and amenities like medical facility, canteen services, business centres

Some of the requirements/ stipulations for a FTWZ are as follows:

- Minimum area to be developed under FTWZ is 40 hectares with a built-up area of not less than 0.5 million sqm
- Minimum outlay for development is over Rs. 9 billion.
- Supply of material into FTWZ to be treated as physical exports for the Domestic Tariff Area (DTA) suppliers
- Hundred per cent FDI allowed for the development of these zones
- Duty-free import/domestic procurement of goods
- Packing or re-packing without processing and labeling as per customer or marketing requirements to be undertaken within the FTWZ
- Principally governed by the SEZ Act 2005 and SEZ rules 2006
- Free foreign exchange currency transactions

With FTWZs, the government expects to generate more employment opportunities as a result of increased

organised warehousing activity due to increased competitiveness among industries in turn boosting the economy.

Central Warehousing Corporation (CWC)

CWC is a premier Warehousing Agency in India, established during 1957 providing logistics support to the agricultural sector, is one of the biggest public warehouse operators in the country offering logistics services to a diverse group of clients.

CWC has 17 Regional Offices in the country. CWC is operating 465 Warehouses across the country with a storage capacity of 10.8 million tonnes providing warehousing services for a wide range of products ranging from agricultural produce to sophisticated industrial products.

Warehousing activities of CWC include foodgrain warehouses, industrial warehousing, custom bonded warehouses, container freight stations, inland clearance depots and aircargo complexes.

Apart from storage and handling, CWC also offers services in the area of clearing & forwarding, handling & transporation, procurement & distribution, disinfestation services, fumigation services and other ancillary activities.

CWC also offers consultancy services/ training for the construction of warehousing infrastructure to different agencies.

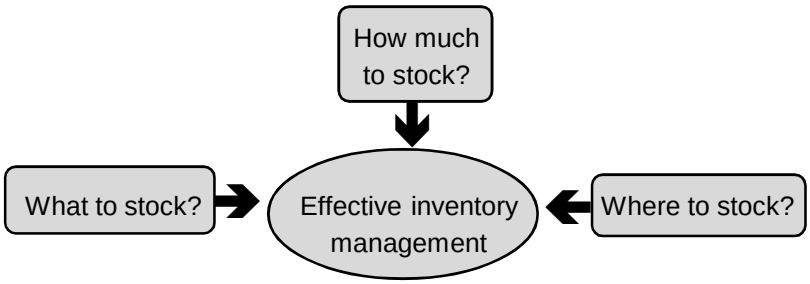
Functions

- The Central Warehousing Corporation may acquire and build godowns and warehouses at such suitable places in India as it thinks fit as per the Warehousing Corporation Act, 1962.
- Run warehouses for the storage of agricultural produce, seeds, manures, fertilizers, agricultural implements and notified commodities offered by individuals, co-operative societies and other institutions;
- Arrange facilities for the transport of agricultural produce, seeds, manures, fertilizers, agricultural implements and notified commodities to and from warehouses;
- Subscribe to the share capital of a State Warehousing Corporation;
- Act as agent of the Government for the purposes of the purchase, sale, storage and distribution of agricultural produce, seeds, manures, fertilizers, agricultural implements and notified commodities; and
- Carry out such other functions as may be prescribed.

CWC operations include scientific storage and handling services for more than 400 commodities including agricultural produce, industrial raw-materials, finished goods and variety of hygroscopic and perishable items. It provides import and export warehousing facilities at its 36 Container Freight Stations in ports and inland stations. It also provides bonded warehousing facilities, disinfestation services and handling, transportation & storage of ISO Containers.

CWC enables the movement of imported and exportable goods to and from the port towns and has developed infrastructure of Container Freight Stations & Inland Clearance Depots throughout the country. It operates 36 CFSs/ ICDs where composite services for containerised movement of import/export cargo are provided. The Warehousing Corporation is empowered to acquire and build Warehouses for storage of Agricultural produce, seeds, fertilizers and other notified commodities and also to act as an agent of the Central Warehousing Corporation or of the Government, for the purpose of purchases, sales storage, distribution etc., of Agricultural Commodities in time of need.

INVENTORY MANAGEMENT



Effective inventory management is all about knowing what to stock, how much to stock and where to stock.

Inventory management is the process of efficiently overseeing the constant flow of units into and out of an existing inventory. This process usually involves controlling the transfer of units in order to prevent the inventory from becoming too high, or dwindling to levels that could put the operation of the company into jeopardy. Competent inventory management also seeks to control the costs associated with the inventory, both from the perspective of the total value of the goods included and the tax burden generated by the cumulative value of the inventory.

Successful inventory management involves creating a purchase plan that will ensure that items are available when they are needed (but that neither too much nor too little is purchased) and keeping track of existing inventory and its use. Two common inventory-management strategies are the just-in-time method, where companies plan to receive items as they are needed rather than maintaining high inventory levels, and materials requirement planning, which schedules material deliveries based on sales forecasts.

Balancing the various tasks of inventory management means paying attention to following aspects of any inventory:

- The first aspect has to do with time. In terms of materials acquired for inclusion in the total inventory, this means understanding how long it takes for a supplier to process an order and execute a delivery. Inventory management also demands that a solid understanding of how long it will take for those materials to transfer out of the inventory be established. Knowing these two important lead times makes it possible to know when to place an order and how many units must be ordered to keep production running smoothly.
- Calculating what is known as buffer stock is also key to effective inventory management. Essentially, buffer stock is additional units above and beyond the minimum number required to maintain production levels. For example, the manager may determine that it would be a good idea to keep one or two extra units of a given machine part on hand, just in case an emergency situation arises or one of the units proves to be defective once installed. Creating this cushion or buffer helps to minimize the chance for production to be interrupted due to a lack of essential parts in the operation supply inventory.
- Inventory management is not limited to documenting the delivery of raw materials and the movement of those materials into operational process. The movement of those materials as they go through the various stages of the operation is also important. Typically known as a goods or work in progress inventory, tracking materials as they are used to create finished goods also helps to identify the need to adjust ordering amounts before the raw materials inventory gets dangerously low or is inflated to an unfavorable level.
- Finally, inventory management has to do with keeping accurate records of finished goods that are ready for shipment. This often means posting the production of newly completed goods to the inventory totals as well as subtracting the most recent shipments of finished goods to buyers. When the company has a return policy in place, there is usually a sub-category contained in the finished goods inventory to account for any returned goods that are reclassified as refurbished or second grade quality. Accurately

maintaining figures on the finished goods inventory makes it possible to quickly convey information to sales personnel as to what is available and ready for shipment at any given time.

In addition to maintaining control of the volume and movement of various inventories, inventory management also makes it possible to prepare accurate records that are used for accessing any taxes due on each inventory type. Without precise data regarding unit volumes within each phase of the overall operation, the company cannot accurately calculate the tax amounts. This could lead to underpaying the taxes due and possibly incurring stiff penalties in the event of an independent audit

PACKAGING

Packaging can be described as a coordinated system of preparing goods for transport, warehousing, logistics, sale, and end use. Packaging is the science, art, and technology of enclosing or protecting products for distribution, storage, sale, and use. Packaging also refers to the process of design, evaluation, and production of packages. Packaging contains, protects, preserves, transports, informs, and sells. Packaging is done to fulfill following objectives-

1. ***Physical protection*** – The objects enclosed in the package may require protection from mechanical shock, vibration, electrostatic discharge, compression, temperature, etc.
2. ***Barrier protection*** – A barrier from oxygen, water-vapour, dust, etc., is often required. Keeping the contents clean, fresh, sterile and safe for the intended shelf life is a primary function.
3. ***Containment or agglomeration*** – Small objects are typically grouped together in one package for reasons of efficiency. For example, a single box of 1000 pencils requires less physical handling than 1000 single pencils. Liquids, powders, and granular materials need containment.
4. ***Information transmission*** – Packages and labels communicate how to use, transport, recycle, or dispose of the package or product. With pharmaceuticals, food, medical, and chemical products, some types of information are required by governments. Some packages and labels also are used for track and trace purposes.
5. ***Marketing*** – The packaging and labels can be used by marketers to encourage potential buyers to purchase the product. Package graphic design and physical design have been important and constantly evolving phenomenon for several decades. Marketing communications and graphic design are applied to the surface of the package and (in many cases) the point of sale display.
6. ***Security*** – Packaging can play an important role in reducing the security risks of shipment. Packages can be made with improved tamper resistance to deter tampering and also can have tamper-evident features to help indicate tampering.
7. ***Anti-counterfeiting Packaging*** – Packages can be engineered to help reduce the risks of package pilferage or the theft and resale of products: Some package constructions are more resistant to pilferage and some have pilfer indicating seals. Counterfeit consumer goods, unauthorized sales (diversion), material substitution and tampering can all be prevented with these anti-counterfeiting technologies. Packages may include authentication seals and use security printing to help indicate that the package and contents are not counterfeit.
8. ***Convenience*** – Packages can have features that add convenience in distribution, handling, stacking, display, sale, opening, reclosing, use, dispensing, reuse, recycling, and ease of disposal.

Packaging types

Packaging may be looked at as being of several different types. On the basis of function packaging can be of following types:

- Primary packaging is the material that first envelops the product and holds it. This usually is the smallest unit of distribution or use and is the package which is in direct contact with the contents.
- Secondary packaging is outside the primary packaging, perhaps used to group primary packages together.
- Tertiary packaging is used for bulk handling, warehouse storage and transport shipping. The most common form is a palletized unit load that packs tightly into containers.

CONTAINERISATION/UNITIZATION

An important part of packaging as it relates to storage and material handling is the concept of unitization. Unitization describes the physical grouping of master cartons into one restrained load for material handling or transport. The concept of containerization includes all forms of unitization. All types of containerization has one basic objective of increasing material handling efficiency. ***Unitisation / Containerisation is the technique or practice of stowing freight in reusable containers of uniform size and shape for transportation. The freight may sometimes be oddly shaped and in different quantities. But when stowed and shipped in containers, it can be handled as a single piece thus making it a lot easier to transport which in turn reduces the time and costs involved.***

Containerisation also enables inter modal transport i.e. the total movement from the origin to the destination using different modes en-route like roadways, railways, shipping, airlines etc. It could be either a combination of several or even just two of these modes.

Before containerisation, cargo would have had to be loaded on a truck piece by piece and driven to a port and there at the dock side each piece would be individually unloaded and then hoisted onto the ship. This was a cumbersome process and consumed a lot of time. Ships often needed to be in port for 10 days to complete the process of unloading and loading.

With the arrival of containerization, shippers started stuffing their goods into containers and deliver them to the port container yard for shipment. The vessels calling the port could unload and load containers and sail within a day to two depending on the number of boxes to be handled.

Containerisation can be defined as a system of inter modal freight and cargo transport using standard ISO containers (known as Shipping Containers or Isotainers) that can be loaded and sealed intact onto container ships, railroad cars, planes and trucks.

The use of containers began in the early 1950's with purpose-built container ships being launched in Denmark in 1951. During the first twenty years of growth containerization meant using completely different, and incompatible, container sizes and corner fittings from one country to another. There were dozens of incompatible container systems used throughout the world. The standard sizes and fitting and reinforcement norms that exist now evolved out of a series of compromises between international shipping companies, European railroads, U.S. railroads, and U.S. trucking companies. The bulk of the discussions occurred in the late 1960s and the first draft of the resulting ISO standards were prepared for publication in 1970. Four important ISO recommendations standardized containerization globally:

- January 1968 - R-668 defined the terminology, dimensions and ratings
- July 1968 - R-790 defined the identification markings
- January 1970 - R-1161 made recommendations about corner fittings
- October 1970 - R-1897 set out the minimum internal dimensions of general purpose freight containers

Over the past fifty years, the use of containers have revolutionised freight handling and helped to grow international trade. Almost every manufactured product consumed today spends some time in a container. Today, approximately 90% of non-bulk cargo worldwide moves by containers stacked on transport ships.

Thus Containerisation involves the unitizing of cargo through the use of standard metal containers and is used by both shipping lines and air cargo lines. Containers provide cargo protection from weather, damage, and theft, and have helped reduce logistical costs and increase the growth of trade.

Container

The container is also known as Freight Container or Shipping Container or Cargo Container or Isotainer. According to ISO a freight container is an article of transportation

- of a permanent character & accordingly strong enough to be suitable for repeated use
- specially designed to facilitate the carriage of goods by one or more modes of transport, without intermediate reloading
- fitted with devices permitting its ready handling particularly its transfer from one mode of transfer to another
- so designed as to be easy to fill and empty
- having an internal volume of 1 m3 or more.

A cargo container is a large container for freight. Cargo containers can be loaded onto container ships, planes, railroad cars, and trucks. Most cargo containers are used to carry just about anything-from cotton to meat to toys. The goods shipped most likely will fall under one of three categories:

- **Refrigerated cargo** includes such items as seafood, fruit, vegetables, and poultry. Refrigerated cargo containers are equipped with a special refrigeration unit that can be set to a specific temperature for a desired duration. Refrigerated cargo containers can even be set cold enough to ship ice.
- **Dry cargo** containers that are used to transport items such as clothing, lumber, computers, and toys are called bulktainers.
- **Dangerous and hazardous cargo** includes chemical-based and/or flammable goods, such as liquefied compressed gasses, liquefied petroleum gas, ammonia, and pharmaceuticals. Steel drums, plastic drums, tanks, gas bottles, and intermediate bulk containers are used to transport goods deemed "dangerous."

Types of containers

Containers come in different size, types and shapes.

By Size – Even though the International Standards Organisation (ISO) has approved certain external dimensions of general-purpose containers, many additional dimensions exist. Essentially there are five main lengths of containers; they are: 20 ft, 40 ft, 45 ft, 48 ft and 53 ft (note that container sizes are often still given in feet and inches and refer to the outside dimensions of the container). Besides for these lengths, there are two common heights, namely 8 ft 6 in and 9 ft 6 in (the last-mentioned is referred to as a high-cube container). Most of these containers are 8 ft wide, although the 48 ft and 53 ft containers can be 8 ft 6 inches in width. The 48 ft and 53 ft containers are not used in shipping and are generally confined to truck and rail use in the US. The 20 ft, 40 ft and 45 ft containers are common in trade throughout the world, with the first two being the most common. The dimensions of these last-mentioned containers are provided in the table below:

Type of container	***Length (internal)***	***Width (internal)***	***Height (internal)***	***Carrying capacity***
6m/20ft GP container	5,90 m (19’ 3")	(2,34 m (7’ 7")	2,38 m (7’ 8")	21 640 kg (47 716 lbs) maximum weight
12m/40Ft GP Container	12,01 m (39’ 3")	2,33 m (7’ 7")	2,38 m (7’ 8")	26 500 kg (58 433 lbs) maximum weight
12m/40Ft GP High-Cube Container	12,01 m (39’ 3")	2,33 m (7’ 7")	2,69 m (8’ 8")	26 330 kg (58 058 lbs) maximum weight
14M/45Ft GP Container	13,58 m (44’ 6")	2,35 m (7’ 7")	2,69 m (8’ 8")	28 390 kg (62 589 lbs) maximum weight

By construction –

- ***Dry Van (standard height):*** General purpose completely enclosed weatherproof container.
- ***Dry Van (high cube):*** Adds an additional foot to the typical interior height of containers.
- ***Dry Van (half-height):*** Reduced height container. This is typically more favorable because of reduced rates.
- ***Open-Top Container:*** A container with a fitted removable roof, or a tarpaulin roof, so the container can be loaded or unloaded from the top used for bulk minerals, heavy machinery.
- ***Open-Side Container:*** Open-sided containers that have end bulkheads. When the rack is empty, the containers can be folded down for loading oversize pallet.
- ***Side-Door Container:*** A container fitted with a rear door and a minimum of one side door.
- ***Refrigerated Container:*** A container with a refrigeration unit. Temperature is controlled from -25°c to +25°c.
- ***Auto Rack:*** A specialized piece of railroad rolling stock used to transport automobiles from factories to dealerships.
- ***Flat-Rack:*** A flatbed with fixed ends for the transportation of cargo of excessive width and weight.
- ***Bulktainer:*** Any container used to transport dry goods.
- ***Tank:*** A container, typically large and metallic, used to transport liquid goods and dangerous goods.
- ***Gas Bottle:*** Cylindrical container used to transport gas.
- ***Swapbody:*** A container equipped with adjustable support legs that allow the container to load onto the vehicle quickly and easily.
- ***High cube palletwide containers f***or europallet compatibility
- ***Flushfolding flat-rack containers*** for heavy and bulky semi-finished goods, out of gauge cargo.
- ***Platform or bolster for barrels and drums***, crates, cable drums, out of gauge cargo, machinery, and processed timber
- ***Ventilated containers*** for organic products requiring ventilation.
- ***Rolling floor*** for difficult to handle cargo.

Container Unit - 'Teu' Twentyfoot Equivalent Unit

Container capacity is measured in twenty-foot equivalent units (TEU, or sometimes TEU). A twenty-foot equivalent unit is a measure of containerised cargo capacity equal to one standard 20 ft (length) × 8 ft (width) × 8 ft 6 in (height) container. In metric units this is 6.10 m (length) × 2.44 m (width) × 2.59 m (height), or approximately 39 m^3.

Most containers today are of the 40-ft (12.2 m) variety and are known as 40-foot containers. This is equivalent to 2 TEU. 45-foot (13.7 m) containers are also designated 2 TEU. Two TEUs are equivalent to one forty-foot equivalent unit (FEU). High cube containers have a height of 9 ft 6 in (2.9 m), while half-height containers, used for heavy loads, have a height of 4 ft 3 in (1.3 m). When converting containers to TEUs, the height of the containers typically is not considered.

The maximum gross mass for a 20-ft dry cargo container is 24,000 kg, and for a 40-ft, (inc. the 2.87 m (9 ft 5 in) high cube container), it is 30,480 kg. Allowing for the tare mass of the container, the maximum payload mass is there reduced to approximately 21,600 kg for 20-ft, and 26,500 kg for 40-ft containers.

Container Seal Numbers

All containers have a four letter and a seven number identification, which is unique to that container. When receiving a container for packing the exporter should always record this number for documentation purposes. Example of a container number: MEAU 9939825.

The container seal is provided by the shipping lines and serves as a lock for securing the container. Each seal has a unique number and the shipper should also record this number on all documentation pertinent to the shipment. Upon arrival of the container at the final destination, should the seal number not correspond with the documentation, the importer should immediately notify the shipping line and the marine insurance company.

Concepts of FCL & LCL

FCL means Full Container Load. Here the container consists of cargoes meant for one party, i.e. consignee only. The cargo is stuffed at shipper's warehouse and is de-stuffed at consignee's warehouse. Here the responsibility of stuffing, stowing of cargo inside the container is of the shipper. Stuffing charges are on account of the shipper and the de-stuffing charges on account of the consignee.

LCL means Less Container Load. Here the container consists of cargoes meant for different parties. The carrier collects cargoes from various shippers and stuffs all of them into a container at the pier. At destination, the carrier's agents de-stuff the cargoes from the container and deliver the cargoes to respective consignees.

FCL/LCL means a shipment of goods in which the merchant is responsible for packing into the container and the carrier is responsible for unpacking the container.

LCL/FCL means a shipment of goods in which the carrier is responsible for packing into the container and the merchant is responsible for unpacking out of the container.

Procedure for Selection of the Container

First of all selection of container would depend on the type of cargo. Then calculate the quantity of cargo that needs transporting. Now, depending on the quantity, which sized containers would best suit the needs would be decided. The length of most cargo containers are 10 ft., 20 ft., 30 ft., 40 ft., 45 ft., 48 ft., and 53 ft. Containers that are 20 ft and 40 ft in length are commonly used in ocean freight. Standard width of these containers are 8 ft, while standard height is 8.5 ft. Containers are also available as half height (approx. 4.3) or as high cube (9.5 ft.). One has to make sure that the weight of the cargo does not exceed the containers' rating, which is the maximum permissible weight of a container plus its contents. Now choose the container type from the options available.

Factors to consider in choosing a cargo container include cost and the convenience of loading and unloading cargo. It is also necessary to ensure that the cargo containers one decides to use meets all federal and international regulations. Containers should be properly labeled and have proper documentation. Especially tight restrictions are in place concerning the transportation of hazardous and dangerous cargo. There are numerous laws regulating the carriage of cargo on state and international levels. Laws are also specific to the type of cargo carried.

Container Ship

Ocean going ship designed to carry containers both internally and on deck. Some are self sustaining.

Container Yard (CY)

The term CY means the location designated by Carrier in the port terminal area for receiving, assembling, holding, storing and delivering containers, and where containers may be picked up by shippers or re-delivered by consignees. No container yard (CY) shall be a shipper's, consignee's or a forwarder's place of business, unless otherwise provided.

Container Terminal

A container terminal is a facility where cargo containers are transshipped between different transport vehicles, for onward transportation. The transshipment may be between ships and land vehicles, for example trains or trucks, in which case the terminal is described as a maritime container terminal. Alternatively the transshipment may be between land vehicles, typically between train and truck, in which case the terminal is described as an inland container terminal.

Maritime container terminals tend to be part of a larger port, and the biggest maritime container terminals can be found situated around major harbours. Inland container terminals tend to be located in or near major cities, with good rail connections to maritime container terminals.

Both maritime and inland container terminals usually also provide storage facilities for both loaded and empty containers. Loaded containers are stored for relatively short periods, whilst waiting for onward transportation, whilst unloaded containers may be stored for longer periods awaiting their next use. Containers are normally stacked for storage, and the resulting stores are known as container stacks.

Thus Container terminal is a seaport having facilities for:

- Berthing of container vessels
- Loading / discharge of containers on / from vessels / trucks / railway
- Area for storage of import / export containers
- Good land connection by way of roads / rail

Sequence of Operations & Documentation Procedures in Container Terminal

- Filing of Vessel Identification Advice (VIA)
- Designation & preparation of yard to receive containers
- Accepting the receipt of containers
- Receiving & stacking the containers
- Cut-off time
- Updation of yard
- Receipt of Advance List, Inbound stowage & Export stowage

- Preparation of import/export plan
- Execution of operations

Benefits of Containerisation

- Reduction in port time
- Improved working ratio of ships
- Savings in packing cost
- Reduction in inland transportation cost
- Less transit time & consequent less inventory cost
- Less damage & pilferage of cargo
- Increased efficiency
- Greater security
- Economical shipping costs

Containersation in India

- The concept of containerisation was introduced in India in 1968 in a seminar held in Mumbai. Since then the Indian ship owners and the trade started considering its use. A working Committee report on the subject came out. Sometime in early 1970s, the Shipping Corporation of India Limited acquired its first semi-container ship with three holds designed to carry containers and other two holds to carry general cargo. Other shipping companies like Scindias and India Steamship followed suit. Later, India Steamship Company acquired a small cellular container ship.
- Hi-tech advancement of affording minimum packing to containerised cargo with special applications / coatings to prevent moisture, deterioraion, damage, etc., to cargo is available now to the Indian Exporter.
- Jawaharlal Nehru Port Trust, Navi Mumbai, has introduced a system by which inspection of containers is much faster than manual, thereby reducing congestion.
- The inherent advantages of moving cargo through containers (lesser wastage, faster delivery), combined with increased capacities at ports is expected to increase container penetration from current level of 16% to above 21% by 2012 as per Goldman Sachs Report, May 2008.
- The US based USI's electronic cargo inspection system is introduced in key ports.
- Out of 46,222 ships, general cargo ships were 18,150; container ships were 3165.
- While 70% of goods movement is containerised globally, its 30-35% in India.
- Container cargo movement is undertaken by private parties also and they are allowed to tranship export cargo to container cargo carrying export cargo to ICD. This flexibility avoids transhipment. This is export facilitation measure.

Container Corporation of India Ltd.

Container Corporation of India Ltd. (Concor) is a Category I Miniratna Public sector undertaking under the Indian Ministry of Railways. Incorporated in March 1988 under the Companies Act, Concor commenced operations in November 1989 taking over an existing network of seven inland container depots (ICDs) from Indian Railways.

From its humble beginning, it is now an undisputed market leader having the largest network of 62 ICDs/CFSs in India. In addition to providing inland transport by rail for containers, it has also expanded to cover management

of Ports, air cargo complexes and establishing cold-chain. It has and will continue to play the role of promoting containerization of India by virtue of its modern rail wagon fleet, customer friendly commercial practices and extensively used Information Technology. The company developed multimodal logistics support for India's International and Domestic containerization and trade. Though rail is the main stay of our transportation plan, road services and also provided to cater to the need of door-to-door services, whether in the International or Domestic business.

CONCOR's customs bonded Inland Container depots are dry ports in the hinterland, and serve the purpose of bringing all port facilities including Customs clearance to the customer's doorstep. The terminals are almost always linked by rail to the Indian Railway network, unless their size or location dictates that they be linked by road. CONCOR's terminals provide a spectrum of facilities in terms of warehousing, container parking, repair facilities, and even office complexes. As CFS operator, CONCOR adds value to the logistics chain by offering value added services such as

- Transit warehousing for import and export cargo
- Bonded warehousing, enabling importers to store cargo and take partial deliveries, thereby deferring duty payment.
- Less than Container Load (LCL) consolidation, and reworking of LCL cargo at nominated hubs
- Air cargo clearance using bonded trucking

CONCOR is using various online applications like Export/Import Terminal Management System (ETMS), Oracle Financials-ERP, etc. Facility for electronic filing (e-filing) of commercial documents of CCLS(Container and Cargo Logistic System) has been provided to customers. This facility enables customers like Shipping lines, Importers, Exporters and CHA's to file the required documents online for process and take necessary printouts of processed output through web from anywhere without physically coming to ICD.

CONCOR has its own WebServer for providing web interface to the commercial applications i.e. ETMS, CCLS, DTMS etc. The web interface enables our customers to access information regarding their shipments by means of the website.

An integrated track and trace system was also implemented on CONCOR website for providing Container Tracking Details.

CONTROL AND COMMUNICATION

The logistics control system consolidates the data of defined subsystems, thereby allowing processes to be visualised, both within a production location as well as beyond company boundaries.

Employing information technology as a means to enhance supply chain competitiveness is an ongoing challenge for both supply chain and information technology (IT) executives. The typical supply chain related applications include enterprise resource planning (ERP), warehouse management systems (WMS) and transportation management systems (TMS). These applications represent standardized processes that should focus on accuracy, consistency, economies of scale and efficiency.

The Role Information Technology in Logistics

The logistics information system (LIS) is a subsystem of the Management Information System (MIS). It provides the information that is specifically needed for logistical management at four levels.

- First, the lowest level of the pyramid refers to transactions and inquiries. Examples of these activities are order inquiries, order processing, stock status checks, bill of lading preparation, and transportation rate look ups. Such interactions with the system occur as frequently as many times an hour, and speed

of the information flow is highly important. Operative personnel such as order-processing and transportation-rate clerks are typical users at this level.

– Second, the next higher level use of the information systems involves first line supervision. Warehouse supervisors must exercise control over space control over space utilization, inventory, and labour productivity in order-filling operations. A truck-fleet manager must have the necessary people, equipment and spare parts to accomplish the transportation mission and schedule deliveries.

– Third, tactical planning and control is an extension of management at supervisory level in that it concerns planning that is often repeated in less than one year. Evaluation of inventory control limits, supplier evaluation, carrier selection, planning warehouse layout, and planning for seasonal space and transportation needs are examples of technical planning and control problem. These tasks can frequently involve middle management such as the manager of physical distribution or manager of transportation.

– Finally, strategic (long-range) planning involves setting the goals, policies and objectives. Deciding on the overall logistical structure and determining the resources needed for the supply distribution task. Speed of information availability is rarely critical, and the information system is interrogated infrequently. Manual procedures and off line computer storage of the necessary information usually prove satisfactory for this level of planning.

For logistics information system, it is necessary to have appropriate database, data retrieval procedures, data processing programme and data analysis. Data for logistics management comes from different sources and in different forms which is recorded manually and in computer files. Appropriate decision for the methodology of data storage, retrieval and criticality of the information should be decided.

The application of IT can support logistics and help in resolving several problems. Over and above assisting in managerial tasks such as planning, deciding on the optimal route of transportation and allocation, distribution, etc. IT can play a vital role in logistics.

(1) Sales Order Processing and Invoicing: Many distribution operations serve highly competitive market. Hence, it is essential that the information about sales order is transmitted by sales office to the distribution department in an efficient manner for dispatch. Information technology plays a key role in the controlling the order cycle, dispatch and raising invoice by accounts for customers. Information technology also helps accounting for necessary controls over payments from different customers.

(2) Warehousing and Stock Control: Integration of stock records, sales order processing, replenishment of stocks and locations of different products at different warehouses are controlled through it. It helps in transfer of stocks from one location to another to reduce inventory and provide customers services in cost effective manner. It also helps in providing the exact information out delivery schedule, and a multi product company at multi-location is able to quickly initiate steps for correlating production and customers requirement.

(3) Fleet Management: Information technology assists in vehicle routing, scheduling, fleet management, computerized round planning is used to evaluate, distribution, fleet mix, provide costing to evaluate alternative distribution networks. Successful implementation of computerized round planning system realize on accurate and timely information about order processing, cost control, order consolidation, distribution constituents like access restrictions, lunch time closing, etc.

(4) Tracking goods in transit: One of the major problems in logistics has been lost and untracked parcels thereby affecting inventory policies, etc. Real time tracking of goods throughout the supply chain provides excellent opportunities for improving customer service. Real time information on delivery time supports just-in-time manufacture and retail, enabling organizations to make strategic decisions with full confidence in the availability of goods. Goods tracking is also important for direct end-customer service. Several leading package delivery companies are offering parcel tracking via the Internet as a fundamental element

of the service. There are many additional areas where accurate, real-time goods tracking can deliver significant improvements. For example, lost luggage is estimated to cost the airline industry in excess of $100 million annually. Any improvements in this area not only reduce the cost of compensation payments to customers but also significantly improve customer service. The standard way to identify and follow a product on its journey through factories and down the supply chain has long been the familiar bar code. However, bar codes have a lot of problems and the use of bar codes also requires a lot of labour. According to industry figures, as many as 60% of the workers in warehouses spend time validating bar codes. Items have to be lined up individually for scanning, even in highly automated identification systems such as those at major package-handling firms. Companies the world over are trying smart tags, specifically, ratio frequency identification (RFID) for tracking parcels and other goods.

Emerging Trends in Application of IT for Logistics Management

1. Radio Frequency Identification (RFID): Radio frequency stands for electromagnetic waves of a wavelength suitable for wireless communication. The RFID system uses a plastic tag, sometimes as small as two matches laid side by side. Embedded in it is a digital memory chip the size of a pinhead. The tag contains information about the product, viz., its origin, its destination, etc. In bar codes, products have to be properly aligned to the scanner for reading the information stored on it. However, this is not a problem with RFID as radio is used. One major advantage with these radio tags is that without touching or removing the tag, a user can alter the information on it. From changing the itinerary of a component on the factory floor to breaking this information in parts, to actually changing the entire information, all of this can be done without touching or going near the tags. The tiny RFID tag has an antenna of its own, a loop of copper plating. This antenna helps a remote device perform the read/write operations. By using RFID tags throughout the supply chain, configure-to-order assemblers could close coordinate the arrival of components for final assembly.

RFID can allow the manufacturer schedule productions as he can know in advance exactly when the shipment is due and when the products are arriving.

2. Distribution Resource Planning (DRP): Distribution resource planning (DRP) is a general framework for planning and managing inventory in distribution networks. The DRP framework can be applied to complex distribution networks with thousands of unique stock-keeping units and hundreds of stocking locations.

DRP determines the need to replenish inventory at branch warehouse. It provides with a time-phased order requirements by date. The overall intent of DRP is to schedule inventory levels specified by management policies. DRP is a push system managed from a central location. Some companies may prefer to the use decentralized decision making at each warehouse, replenishing stock based on warehouse orders using local re-order points.

An advanced version of DRP is DRP II which is a planning philosophy which permits the planning of all resources within a distribution firm including business planning, marketing/sales, procurement, logistics, distribution requirements and financials. The system logic provides the means to define a business plan, a marketing plan, a forecast and a master delivery schedule (master schedule) and focus resources upon a common game plan and related performance measurements. DRPI and DRPII have a similar relationship for managing distribution operations as MRPI and MRPII have for managing manufacturing resources.

3. Geographical Information Systems (GIS): Geographical Information Systems (GIS) enable storage, manipulation, analysis and display of geographically referenced data. The rate of growth in the GIS industry has accelerated in the 1990s as businesses have adopted GIS to relate different sources of information to one another through a common geographical reference. The value of GIS lies in enabling users to integrate different sets of data through a common geographical reference system such as latitude and longitude, easting's and northings or a common pre-defined geography such as postal codes, etc. User can then interrogate these data based on their geographical relationships and display the results on a map, in a table or on a chart.

The greatest challenge of logistics is a routing of vehicles especially in India as the geographical spread is fairly

large. GIS can simplify this task by reducing the complexity by bringing out subtle geographic patterns and relationships that can form the basis of good decisions. Some of the other applications of GIS in logistics are:

(a) Vehicle tracking and dispatch involves being able to keep track of the location and the inventory on board every vehicle in the field and having the latest information on its position and operating status.

(b) Route analysis is the operation which aims at minimizing the cost of travel involved in transporting goods from one location to another whether in terms of trips required or time or distance or a combination of these.

(c) Warehouse operations become significant in cost reduction when the operation grows big and each warehouse becomes a very large operation in itself.

(d) Facilities and depot management involves minimizing waste by considering the locational aspects, the available capacity, the inventory in question and the range or effective covered area of each facility.

(e) Routing and scheduling aims at minimizing all kinds of costs including mileage, overtime and maximizing all attendant benefits including customer satisfaction, adherence to schedules, etc.

Global positioning systems or GPS are becoming cheaper, more cost effective and widespread. If the trucks are fitted with radio transmitters and GPS, the radio transmitters and GPS, the radio transmitters send the location of the truck at specific intervals to the central control, where GIS software interprets the signal and posts it on the two map as symbol. This enables the dispatcher to track the location of this truck and the rest of the fleet in real time. Along with other information such as traffic movement, etc. the dispatcher should also be able to leverage the real time traffic conditions to modify the route the truck could or should take to minimizes delays.

A route analysis system of GIS has the ability to use information pertaining to route density and could utilize this kind of data to generate the most efficient routes that any vehicle should take based on the current inventory load it is carrying. The system can also help the driver find the address by generating map and providing the driving directions.

The system can also be joined to an inventory control system in ERP software like SAP R/3 which could help create geographically aware inventory ‘packets’ for delivery, taking into account the locations of the address and the capability of the truck that will service the specific route.

Though currently there are several constraints in India such as getting information related to route density, etc. we are not far away from being able to utilize GIS optimally in logistics.

LESSON ROUND UP

- Logistics management is the process of planning, implementing and controlling the efficient, effective flow and storage of goods, services and related information from the point of origin to the point of consumption for the purpose of conforming to customer requirements.
- Logistics can be inbound or outbound and domestic or international.
- Logistics play a critical role in each of the three critical elements of the marketing concept (customer satisfaction, integrated effort/systems approach and corporate profit) in several ways.
- Transportation provides the flow of materials, products and persons between production facilities, warehouses, distribution centres, terminals and customer locations.
- Rail, road, air, water and pipeline are the five modes of transportation used by logistics management to transport material from one place to another.
- A common carrier is a business that transports people and/ or goods, offers its services to the general public under license or authority provided by a regulatory body.

- Third-party logistics (3PL) refers to outsourcing transportation, warehousing and other logistics related activities to a 3PL service provider that were originally performed in-house.
- 4PL is new concept is supply chain outsourcing. It is the next level in logistics out-sourcing and is considered as a path to achieve more than the one time operating cost reductions and asset transfers of a traditional outsourcing arrangement.
- A warehouse is a commercial building for storage of goods. Warehouses are used by manufacturers, importers, exporters, wholesalers, transport businesses, customs, etc.
- Warehouse Management Systems (WMS) is one of the most significant technologies used for logistics which enables efficient management of material flow, proper tracking of the movement of goods and on-time delivery of goods to customers.
- A logistics park is a stipulated area that facilitates domestic and foreign trade by providing services such as warehousing, cold storage, multi-modal transport facility, CFS, ICDs, etc.
- Free Trade Warehousing Zones (FTWZ) were established by the government to develop infrastructure to facilitate import and export of goods and services with the freedom to carry out trade transactions in the free currency.
- CWC is a premier Warehousing Agency in India, established during 1957 providing logistics support to the agricultural sector, is one of the biggest public warehouse operators in the country offering logistics services to a diverse group of clients.
- Inventory management is the process of efficiently overseeing the constant flow of units into and out of an existing inventory.
- Packaging can be described as a coordinated system of preparing goods for transport, warehousing, logistics, sale, and end use.
- An important part of packaging as it relates to storage and material handling is the concept of unitization.
- Unitization describes the physical grouping of master cartons into one restrained load for material handling or transport.
- Containerisation can be defined as a system of inter modal freight and cargo transport using standard ISO containers (known as Shipping Containers or Isotainers) that can be loaded and sealed intact onto container ships, railroad cars, planes and trucks.
- The container is also known as Freight Container or Shipping Container or Cargo Container or Isotainer Container Corporation of India Ltd.
- (Concor) is a Category I Miniratna Public sector undertaking under the Indian Ministry of Railways. Incorporated in March 1988 under the Companies Act, Concor commenced operations in November 1989 taking over an existing network of seven inland container depots (ICDs) from Indian Railways.
- The logistics control system consolidates the data of defined subsystems, thereby allowing processes to be visualised, both within a production location as well as beyond company boundaries.
- The application of IT can support logistics and help in resolving several problems. Over and above assisting in managerial tasks such as planning, deciding on the optimal route of transportation and allocation, distribution, etc.

SELF TEST QUESTIONS

1. What is logistics management? Explain the role of logistics management in an organisation.

2. Describe briefly different stages of logistics management.
3. What are the different modes of transport available? Explain their advantages and disadvantages.
4. What are the different types of warehouses?
5. What do you mean by containerisation? Explain the types of containers.
6. Describe the role of information technology in logistics management. Also highlight some of the emerging IT concepts being used in logistics management.
7. Write a short note on following-
   - Third party logistics providers
   - Fourth party logistics providers
   - FTWZ
   - Logistics Parks
   - CWC
   - Warehouse management systems

PROFESSIONAL PROGRAMME

INTERNATIONAL BUSINESS – LAWS AND PRACTICES

PP-IB&LP

Open Book Examination in Elective Subjects (Paper - 9) in Module-III of Professional Programme (New Syllabus) Examination

Professional Programme (New Syllabus) offers five elective subjects in Module III, as mentioned herein below, out of which a student has to opt only one subject to study and qualify that suits his aptitude, interest, ability and career goal:

1. Banking Law and Practice
2. Capital, Commodity and Money Market
3. Insurance Law and Practice
4. Intellectual Property Rights-Law and Practice
5. International Business -Laws and Practices.

There is Open Book Examination (OBE) in all the above five elective subjects from June 2014 onwards. However, in all other subjects/modules of Professional Programme (New Syllabus), students would continue to be examined as per traditional pattern of examinations.

This is to inculcate and develop skills of creative thinking, problem solving and decision making amongst students of its Professional Programme and to assess their analytical ability, real understanding of facts and concepts and mastery to apply, rather than to simply recall replicate and reproduce concepts and principles in the examination.

In OBE, the candidates are allowed to consult their study material, class notes, textbooks, Bare Acts and other relevant papers, while attempting answers, as per the requirement of questions. The emphasis throughout is in assessing the students' understanding of the subject, applying their minds, rather than the ability to memorise large texts or rules or law.

Unlike a conventional/typical examination, which assesses how much information candiates have been able to store in their minds, the success in this type of examination depends on the candidate's ability to understand the question, identify inherent issues, application of various techniques, laws, principles, etc. while solving answers with the help of supporting reference material.

Broad pattern of Question Paper for OBE is as follows:

- Each question paper would contain **Six** questions carrying 100 marks
- Question No.1 will be of 50 marks based on case study ranging between 3000-4000 words.
- Question No.2 will be of 30 marks based on study of regulatory framework related to the subject.
- Question No.3-6 will be of 5 marks each covering important topics of the syllabus.

Candidates are not allowed to consult their fellow examinees or exchange their study material/notes, *etc.* with each other in the examination hall.

Candidates are prohibited to bring in any electronic devices, such as laptop, tab, I pad, palmtop, mobile phone, or any other electronic device/ gadget at the examination hall/room. However, they are permitted to use their own battery operated noiseless and cordless pocket calculator with not more than six functions, twelve digits and two memories.

PROFESSIONAL PROGRAMME EXAMINATION (NEW SYLLABUS)

ELECTIVE PAPER 9.5 – INTERNATIONAL BUSINESS - LAWS AND PRACTICES

PRACTICE TEST PAPER

OPEN BOOK EXAMINATION

Time allowed: 3 hours *Max Marks: 100*

Attempt all questions. All questions are compulsory.

Question No. 1

Read the following case and answer the questions given at the end of the case:

Anti-Dumping Investigation Concerning Imports of Vitamin C from USA and Canada

The Designated Authority (herein after referred to as Authority), under the Rules, received written application from M/s. A Chemicals, a unit of M/s. B Enterprises, India Ltd. for and on behalf of domestic industry, alleging dumping of Vitamin-C originating in or exported from USA and Canada.

The Authority issued a public notice initiating anti dumping investigations dated 14 August, 2002 and notice of Preliminary Findings dated 1st November 2002 was published in the Gazette of India, Extraordinary, recommending imposition of Anti Dumping Duty on Vitamin-C originating in or exported from USA and Canada classified under heading 2936.27.00 of the Custom Tariff Act. The Authority provided an opportunity to all interested parties to present their views orally on 15th January 2003. The Authority made available non-confidential version of the evidence presented by various interested parties in the form of a public file kept open for inspection by all interested parties and the comments received on the same was duly considered in Final Findings.

Petitioner's views

(a) *Dumping from Japan, China, European Union and Russia:* The domestic industry was earlier suffering injury from severe dumping by the exporters from Japan, China, European Union and Russia. After imposition of anti-dumping duty against these countries/territories, exporters from USA & Canada started resorting to dumping of subject goods in the Indian market. In view of the above, it was submitted that while examining injury to the domestic industry in the present case, existence of dumping from China, Japan, European Union and Russia causing injury to the domestic industry is required to be considered, particularly in terms of economic parameters affecting domestic industry and impacts of dumped imports on the prices in the market.

(b) *Cumulative assessment of injury:* The parameters laid down under the Rules for cumulative assessment of injury are well met in this case, as

- quantum of imports and dumping margin from each of the subject countries is more than de-minimus;
- cumulative assessment of the effect of imports is appropriate in light of the conditions of competition between the imported article and the like domestic articles.

(c) Petitioner submitted that the following parameter summarizes injury to the domestic industry.

- Imports of subject goods from the subject countries have increased significantly in absolute terms.
- The share of imports from the subject countries in relation to imports of subject goods in India has increased significantly.
- The share of imports from subject countries in relation to demand in India has increased significantly.

(d) Various Economic Parameters affecting domestic industry –

- Production, capacity utilization of the domestic industry which had been increasing till 2000-01 declined during period under investigation.
- The sales volume of the industry has also declined inspite of reduction in selling price.
- The imports forced the domestic industry to sell the product below its fair value, since the domestic industry was forced to match the prices. Thus, the imports forced the domestic industry to undersell the product.
- The landed value of imported material was significantly below the selling price of the domestic industry causing price undercutting in the Indian market.
- The domestic industry continues to incur significant financial losses as a result of continued dumping in the Indian Market.
- The dumping margin are not only more than de-minimus, but also very significant.

(e) Duty in US $:

Though the Designated Authority has already recommended antidumping duty in terms of US $, it is submitted that the final duties may also be recommended in terms of US $ only, so that erosion in the quantum of protection does not take place on account of changes in the exchange rate. However, the duties may please be recommended in terms of reference price.

(f) On Product under Consideration

The product involved in the present investigation is Vitamin-C in all its form and derivatives. It is also known as ascorbic acid. It is classified under customs subheading no. 2936.27 under the Customs Tariff Act 1975.

(g) On Like Article

There is no significant difference between the product imported from subject countries and produced by the Indian industry in terms of physical & technical characteristics (or product specifications), manufacturing process, plant & equipment, technology, function and uses, marketing, pricing, tariff classification and customer perception. The goods produced by the petitioners and the product under consideration are substitutable with each other.

(h) On Domestic Industry

The petition was filed by M/s. B Enterprises India Limited. There are two other producers of Vitamin-C in India. M/s. XYZ Limited is the other producer of the product. M/s. ABC Limited had also created capacity for production of subject goods. However the company has suspended production long back. Two producers namely M/s New Search Ltd & M/s Bio Chemicals Ltd. have commenced their production after period of investigation, albeit in small volumes. There are other units, namely M/s Cardo Drugs Ltd. & M/s Ton Pharma which are producing Vitamin-C for export purposes, after the investigation period. The petitioner accounts for major proportion of Indian production and thus satisfies the standing under anti dumping duty rules.

Views of Exporters:

M/s. Albert Mumbai, representing the producer M/s Albert, have indicated that neither the exporter nor its affiliated have received communication regarding the petition and primary investigation for anti dumping duty on Vitamin ‘C’ of USA origin. They requested the Authority to give at least one month extended period for contesting the case to respond to the initiation notice. However, no response was received by the Authority, from the exporter.

Views of Importers/ Users:

- Domestic Industry is importing the final stage intermediate 2 —Ketogluonic Acid from China and their cost of production is substantially lower than the producer in exporting countries.
- There is difference between the technologies adopted by the petitioner and by produced by the subject countries.

AUTHORITY'S POSITION

As regards to claims of nil export from subject country Canada, it is noted that substantial imports have been reported by Directorate General of Commercial Intelligence and Statistics (DGCI & S), Kolkata. Further, DGCI&S, Kolkata, furnished transaction wise details of imports for the period of investigation from Canada. Chennai Customs, also reported that a quantum of 57.95Mt has been imported during the period of investigation, which constituted around 9.5% of total imports, well above the deminimus limit.

Like Articles: The Authority noted that the Vitamin-C produced and sold by domestic industry and those imported from the subject countries have similar characteristics and should be treated as like articles, petitioners have also claimed that there is no significant different in the technology adopted by petitioner and by the producers in these countries. Though, every manufacturer fine-tunes production process according to available facilities and necessities.

Domestic Industry: The petition has been filed by M/s. B Enterprises India Limited having its Registered Office at Baroda-390007. There are two producers of Vitamin C in India. M/s. XYZ Limited is the other producer of the product. Earlier, M/s. ABC Limited had also created capacity from production of Vitamin-C, however, the company is closed. Authority held that the petitioner accounts for major proportion of the Indian production and thus satisfies the standing, under the Rules.

Dumping: To determine the dumping the Authority sent questionnaires to all the known exporters and producers of Vitamin C in Subject Countries. However, none of the exporters except M/s Albert from subject countries responded to the Authority and have not furnished any information in the form and manner prescribed by the Authority. In the circumstances Normal Value has been based on the price information viz price list of one of the producer of subject goods in USA, provided by the domestic industry in accordance with Rule 6(8). The Normal Value for USA and Canada has been determined at US $ *** per Kg.

Export Price: The average export price has been adjusted for commissions, inland freight, overseas freight, packing & handling charges on the basis of best available information and in accordance with Rule 6(8). The export price has been determined at US$ *** per Kg in respect of USA and at US $ *** per Kg in respect of Canada respectively.

Dumping Margin: The authority carried out weighted average ex-factory normal value comparison with the weighted average ex-factory export price in period of investigation, for evaluation of the dumping margin for all the exporter/ producers of the subject country wherever appropriate. The dumping margin for exporter/ producer comes as under:

COUNTRY	NormalValue	ExportPrice	DumpingMargin	D M as a % of Export price
USA	***	***	***	97.80
CANADA	***	***	***	112.26

Injury

- In the instant case, the imports of Vitamin-C from the subject countries have increased significantly in absolute terms, as may be seen from the table below:

Particulars	Unit	1998-99	1999-00	2000-01	2001-02
Imports					
Imports-China*	MT	405.54	227.73	290.67	130.97
Imports-Japan*	MT	312.70	239.70	49.50	1.70
Imports EU and Russia*	MT	267.20	631.60	43.54	16.84
Imports from -Countries attracting duty*	MT	985.45	1099.03	383.70	149.51
USA	MT	63.11	134.76	51.33	230.51
Canada	MT	0.00	7.00	27.40	152.08
USA, Canada	MT	63.11	141.76	78.72	382.58
Imports Other than above	MT	9.36	41.78	18.00	76.31
Total Imports	MT	1057.91	1282.57	480.43	608.41
** Countries already attracting Anti Dumping Duty.*					
Total Domestic Production	MT	269.28	237.25	544.88	456.30
Demand in the Country	MT	1327.20	1519.82	1025.31	1064.71
Market share in Imports					
Countries attracting duty	%	93.15	85.69	79.87	24.57
USA	%	5.97	10.51	10.68	37.89
Canada	%	0	0.55	5.7	25.00
USA, Canada (Total Imports)	%	5.97	11.06	16.38	62.89
Imports from Other countries	%	0.88	3.26	3.75	12.54
Total	%	100.00	100.0	100.00	100.00

- The exporters from the subject countries have reduced the prices significantly, as may be seen from the following table:

Rs. Per KG	1998-99	1999-00,	2000-01	2001-02
USA	280.64	271.80	263.60	244.77
CANADA	–	261.97	268.01	219.06

- The productions of the domestic industry have increased over years till 2000-01, declined in the period of investigation. Authority noted that the sales volume of the industry have declined over the period, the industry has been forced to reduce its prices significantly at the cost of its profitability in view of the dumped imports.
- It is evident from the table below that the selling price of the domestic industry have declined over the years. Selling price have increased marginally in 2000-01 over, 1999-2000, however, the same declined again in the investigation period.

Year	Sales realization Rs. Per Kg.
1998-99	100
1999-2000	91.11
2000-2001	98.44
2001-2002	86.89

- The Authority noted that the dumped imports have forced the domestic industry to reduce its prices in spite of increase in the cost of production.
- The domestic industry has been forced to reduce number of employees.
- Inventories with the domestic industry have declined.
- On the lines of profitability, the domestic industry is suffering continuous cash losses (except 2000-01) from sale of the product due to continued dumping of the product in the market. Further, cash losses which were showing decline till 2000-01 and the domestic industry made cash profit in 2000-01, again turned into cash losses in the investigation period.
- On the lines of changes in production, productivity of the domestic industry increased upto 2000-01. The same has, however, declined again in the investigation period as compared to previous year.
- On the lines of production and sales, growth of the domestic industry was positive upto 2000-01 (even though the same was negative in 1999-2000), the same became negative in the investigation period.
- The domestic industry is finding it difficult to plan fresh investments given that the performance has materially deteriorated.

Causal Link: The Authority held that the material injury to the domestic industry has been caused by imports from the subject countries that are major exporters of Vitamin C to India.

Indian Industry's Interest and other issues: It is recognised that the imposition of anti dumping duties might affect the price levels of the products manufactured using the subject goods and consequently might have some influence on relative competitiveness of these products. However, fair competition on the Indian market will not be reduced by the antidumping measures, particularly if the levy of the anti dumping duty is restricted to an amount necessary to redress the injury to the petitioner companies. On the country, imposition of anti dumping measures would remove the unfair advantages gained by dumping practices, would prevent the decline of the petitioner company(ies) and help maintain availability of wider choice to the consumers of Vitamin-C. Imposition of anti dumping measures would not restrict imports from the subject countries in any way, and therefore, would not affect the availability of the product to the consumers.

Conclusions: The Authority, after considering the foregoing, concluded that

(a) Vitamin-C (Ascorbic Acid) originating in or exported from USA, Canada and has been exported to India below normal value, resulting in dumping:

(b) The Indian industry has suffered material injury

(c) The injury has been caused cumulatively by the imports from the subject countries.

(d) It is considered necessary to impose definitive anti-dumping duty, on all imports of Vitamin-C originating in or exported from USA and Canada.

Accordingly, the Authority has therefore, decided to recommend definitive Anti-dumping Duty to be imposed, on all imports of Vitamin-C and most commonly used synonyms of Vitamin C like Ascorbic Acid, L-Xyloascorbic Acid falling under Custom Heading 2936 originating in or exported from USA and Canada. An appeal against this order shall lie to the Customs, Excise and Gold (Control) Appellate Tribunal in accordance with the Act.

In view of the facts and circumstances given in the case above, answer the following questions:

(a) Determination of dumping is based on two major parameters. Explain these parameters with the help of facts given in the above case.

(b) "Sufficient evidence must be provided to support the contention of material injury." Elaborate keeping in view the above case.

(c) On the facts and circumstances of the case, whether the Designated Authority has followed proper procedure in determining the anti dumping duty to be imposed on the importers. Discuss.

(d) Do you think the anti dumping duties should be imposed on importers? Is it unfair competition or valid defense of the domestic industry? Discuss citing the above case.

(e) What role can WTO play in the antidumping cases? Elaborate on the anti dumping policies of WTO.

(10 marks each)

Question No. 2

Answer all of the following questions.

(a) You are a company secretary of Hindustan Exports Ltd. Explain how will you despatch the leather jackets manufactured by the company to Dubai without paying duty from India.

(15 marks)

(b) The principle problem in analysing different forms of export financing is the distribution of risks between exporter and the importer. Analyse the following export financing instruments in this respect:

i) Letter of credit

ii) Cash in advance

iii) Draft

iv) Consignment

v) Open Account

Question No. 3

India is a huge country with a vast domestic consumer market. Then why Indian firms are targeting international markets? Do you think Indian firms should go global? Critically analyse.

(5 marks)

Question No. 4

Using the comparative advantage trade theory, outline the case for free trade.

(5 marks)

Question No. 5

Some fundamental principles are the foundation of multilateral trading system. Elaborate.

(5 marks)

Question No.6

Logistics management tries to have the "right product", in the "right quantity", at the "right place", at the "right time" with the "right cost". Explain the flow of resources in the process of logistics management.

(5 marks)