

## B. Second meeting of the NMCC held on 15<sup>TH</sup> April, 2005

Dr. V. Krishnamurthy, Chairman, NMCC at the outset extended a warm welcome to all the participants to the second Council meeting. He pointed out that since the last meeting in January 2005, the secretariat of the NMCC been pursuing various points made by the members and have held informal consultations with many of them. In particular, the points made by the Hon'ble Prime Minister were noted and actively pursued upon.

The Chairman mentioned that the Agenda item no.1 specifically brings out the progress made since the first meeting of the NMCC. While the task before the NMCC is formidable and requires a deep study of various aspects, he drew the attention of the members to the decision to formulate a 'Strategy paper'. He emphasized that while a draft 'Strategy paper' prepared with inputs from some members is placed before the Council as Agenda item no.2 for further deliberations, final paper would be drawn-up as a concise document after taking into account all the suggestions made during the meeting.

The Chairman informed the Council that interactions have taken place with some identified Sub-sectors; some more interactions are planned in the near future with other Sub-sectors. The outcome of the deliberations of the meetings of the Sub-sectors is also placed before the Council as Agenda item no.3. He felt that renewed focus on Small and Medium Enterprises is essential to enable them contribute in the manufacturing growth, which is dealt in Agenda item no. 4.

The Chairman highlighted that the subject matter of manufacturing competitiveness is getting the attention of the highest echelons of the government as both the Prime Minister and the Finance Minister have shown their keenness to receive suggestions from the National Manufacturing Competitiveness Council. The expectations are quite high and the Chairman requested the guidance of the members.

Highlighting on the Agenda items, Mr. V. Govindarajan, Member Secretary NMCC, drew the member's attention on the two-pronged approach of preparing a 'strategy paper' and engaging sub-sectors in a dialogue with a view to identifying issues and corrective actions. He pointed out that the NMCC had received extensive inputs from the

members of the NMCC as well as Secretaries to the government who have participated in the sub-group interactions.

The second Council meeting discussed four Agenda items.

The first agenda item: the NMCC's Status Report- Progress since the first meeting of the Council. The following are the highlights of the 1st agenda item:

As a sequel to the deliberations in the first meeting of the Council held on 06.01.2005 and further to the interaction with the Hon'ble Prime Minister, the following points had emerged:

- ❖ the NMCC's should think big and its recommendations should make a difference;
- ❖ India prematurely migrated to Services, with the Manufacturing sector remaining at about 17% and Industry around 26% of GDP;
- ❖ For India, Industrialization did not play its historic role of growing steadily as a percentage of GDP and providing employment to the surplus labour in agriculture;
- ❖ India should have a realistic ambition of increasing the share of manufacturing sector in GDP to that of the East Asia's levels; while doing so, it is essential that attention is paid to employment.
- ❖ It is necessary to make industry a powerful agent, both of growth and employment; Industrial growth has to accelerate and provide more jobs since nearly 10 million people are getting added to the work force annually and agriculture cannot absorb more people;
- ❖ the NMCC should examine the causes for the virtual stagnation in the growth of manufacturing industry in the past and also examine whether the policy framework was the problem and if so what would be the macro-economic policies that require attention to ensure rapid growth of the sector;
- ❖ Quality issues specifically of teachers are important. The government was considering setting up of a knowledge Commission to look into the issues of building quality human capital. National Manufacturing Competitiveness Council should address this issue;

- ❖ With regard to the defence sector, a structured approach to deal with dual applicability of Science and Technology was required;
- ❖ It has to be borne in mind that reduction in taxation, both the tariffs as well as domestic taxes, has to be considered not only from domestic point of view but also keeping in view India's commitments in the regional and global arena. It was also necessary to know that the indirect taxes as percentage of GDP had declined over the last decade and half in India; and
- ❖ There was a need to provide flexibility in labour regulation in order to enable increase employment opportunities and growth. SEZ could provide good example in this regard.

Based on the above observations, the NMCC has initiated a two-pronged action plan viz.

- ✓ *to formulate a draft Strategy paper incorporating various aspects that are required to be attended to in order that manufacturing to grow rapidly to provide employment and*
- ✓ *form sub-groups in respect of various sub-sectors and discuss the issues and take up the recommendations with the concerned for action.*

#### **(i) The National Strategy for Manufacturing - A discussion paper**

In the first Council meeting the NMCC had suggested that a Strategy paper to be prepared incorporating various elements that are required to be attended to in order that the manufacturing sector grows rapidly and achieves significant proportion to GDP also to provide employment. The following 10 elements were identified for attention as a part of the long-term manufacturing strategy and are under discussion for further elaboration:-

- I. Enhance Government focus on manufacturing competitiveness;
- II. Creating conditions for investment in and growth of the manufacturing sector;
- III. Lowering the cost of manufacturing;
- IV. Investing in innovations;
- V. Strengthening education and training at all levels;
- VI. Adoption of global best practices in manufacturing;
- VII. Right market framework, competition and regulation;

- VIII. Issues relating to competitiveness in small and medium industries;
- IX. Competitiveness of public sector manufacturing industries; and
- X. Infrastructure development.

A detailed study in respect of each of these elements among others is being undertaken to bring out a paper "National Strategy for Manufacturing in India". And some of the elements mentioned above are, no doubt, being attended to by the competent wings of Government. NMCC, would, in these areas, co-ordinate with the concerned agencies/departments in order to bring about synergy.

**(ii) Identification of Sectors for Detailed Study in the Immediate Future:**

The NMCC has also initiated to form Sub-Groups in respect of various sub-sectors and discuss the issues and take up the recommendations with the concerned for action. Thus, 12 sub-sectors have been identified to start with, which have immediate potential for Growth and Employment generation. These are :-

- (i) Textiles and Garments;*
- (ii) Leather and Leather goods;*
- (iii) Food Processing;*
- (iv) Gems and Jewellery;*
- (v) Handlooms and Handicrafts;*
- (vi) Chemicals;*
- (vii) Pharmaceuticals;*
- (viii) IT hardware/ Electronics;*
- (ix) Auto Components;*
- (x) Human resource development relating to manufacturing ;*
- (xi) Capital goods industry; and*
- (xii) Paper Industry*

In pursuance of the above two pronged action plan, NMCC has initiated the process of formulating the 'Strategy paper' and accordingly, the following sub-group meetings have been held to identify the issues relating to these sub-sectors:

- 1. Leather and Leather Goods*
- 2. IT, Hardware and Electronics*

3. *Small and Medium Enterprises*
4. *Textiles and Garments*
5. *Food Processing Industries*
6. *Auto Components*
7. *Capital Goods Sector*

Points arising out of these first round discussions were followed up with the concerned for necessary action. Sub-Group meetings relating to Paper Industry, Chemicals Industry and Human Resource requirements of Manufacturing Industry are scheduled to be held in the last week of April, 2005.

One of the important points that came about during the sub-group discussions as also in the discussions with the Industry Associations and others is the need for streamlining of the indirect tax structure. The current year Budget contains a number of announcements in this direction. Some important steps have been taken to reverse the inverted duty structure, rectify the anomalies and reduce duties on import of capital goods. There has been special attention to infrastructure development through creation of a special purpose vehicle to fund infrastructure up to Rs. 10,000 crores. Number of initiatives has also been taken to improve the competitiveness of small and medium industries.

The NMCC also held consultations with individual departmental heads to understand the issues relating to Textiles, Labour, Environment, Small Scale Industries, etc. In respect of small scale industries, a special meeting has been called for addressing the issues of funding of the small scale industries. Follow up action has been initiated in this regard. The NMCC has also made suggestions for adopting a "Mission Mode" for implementing the identified strategies for accelerated growth in Textiles and Garments sector and the Leather & Leather Goods sector, which is under consideration of the Government.

The NMCC has also taken up with the Finance Ministry on the need to give extra focus and boost to the Textiles and Garments Sector, the Leather and Leather Goods Sector and the IT Hardware Sector all of which have an immediate high potential for growth and employment. These have been addressed in the Budget. Finance Minister in his Budget Speech emphasized the importance of manufacturing sector and made the observation that:

*“India should build on its manufacturing capacities and scale them up to global standards. Both the Investment Commission and the National Manufacturing Competitiveness Council have started work in right earnest”.*

During this period, the Government has taken a number of decisions to improve the competitiveness of the Indian Industry and in particular, the manufacturing sector. A number of elements which were identified in the long-term manufacturing strategy paper have been addressed in the Budget of 2005-06. The initiatives contained in the Finance Minister’s speech for promoting growth in these sectors among others is at **Annexure-I**. In addition, the Finance Minister has also announced a Scheme called Manufacturing Competitiveness Programme. He said:

*“Worldwide, it is manufacturing that has driven growth. In order to revive the manufacturing sector, particularly small and medium enterprises, and to enable them to adjust to the competitive pressures caused by liberalization and moderation of tariff rates, I propose to launch a new scheme that will help them strengthen their operations and sharpen their competitiveness. The scheme will be called the “Manufacturing Competitiveness Programme” The design of the scheme will be worked out by the National Manufacturing Competitiveness Council in consultation with the industry.”*

The purpose behind the announcement is to assist the industry, at least partly, in its efforts to restructure and sharpen its competitiveness in the wake of import Competition. The first meeting of a working group for the purpose was held on 1<sup>st</sup> April, 2005 to discuss and firm up the scheme details.

The Second Agenda item: The National Strategy for Manufacturing - A discussion paper. The NMCC during its first meeting on January 6, 2005 had suggested that a strategy paper should be prepared incorporating various elements that are required to be attended to in order that the manufacturing sector grows rapidly and achieves significant proportion to GDP. The following 10 elements were identified for further elaboration:-

*i) Enhance Government focus on manufacturing competitiveness: In view of comparatively low contribution (17%) of manufacturing in the GDP as against about 30 to 35 per cent in the case of growing East Asian economies, it is high time that manufacturing sector gets the focus and attention of the Government it deserves. The importance of manufacturing in the economic growth and employment generation need not be emphasized any more since it is now widely accepted. Therefore, it is of utmost importance that the Government continues its focus on manufacturing. For this purpose, periodic review of progress would be undertaken with a view to making necessary policy changes.*

*(ii) Creating conditions for the growth of the manufacturing sector is essential for making Indian manufacturing competitive. This would require not only firm level efforts by the corporates but also appropriate macro-economic policy support to facilitate and provide congenial conditions by the Government. It is essential that a thorough review of the past policies which discouraged robust growth of manufacturing is undertaken and recommendations made to rectify and improve the conditions.*

*(iii) Indian manufacturing would be competitive only when the cost of manufacturing is low. Therefore, lowering cost of manufacture in India would be one of the prime focus areas to work upon in the council. This would encompass the entire value chain of manufacturing. Identification of areas for cost reduction and efficiency at each level would be a priority.*

*(iv) Investing in innovations is one of the pre-requisites to attain global competitiveness. The experience of the industry has been that being low-tech does not make them globally attractive. Investing in R&D by the corporates and by the Government of India to adopt*

*technology ahead of markets is essential. Prototype development and design innovations would require to be supported. Creation of common testing facilities and Centres of manufacturing technology excellence are essential. Management of these by the beneficiaries themselves would encourage the Indian manufacturing industry to invest in innovations.*

*(v) Strengthening education and training is essential for building human capital for the growing needs of the manufacturing sector. Qualitative growth in skilled manpower is considered essential. This would imply, inter-alia, working together of the industry, the academia and the Government. The efforts to improve human capital have to take into account the needs of not only the domestic market but also the increasing opportunities in the global market. High quality training at collage and university level as well as at the levels of ITI's is essential.*

*vi) Adoption of global best practices in manufacturing is another area which requires attention for ensuring sustainable competitiveness. Bench-marking and standard setting has to begin from building the human resource and extended to the entire value chain.*

*vii) Right market framework, competition and regulation are essential requirements. The Council would work upon these areas and provide appropriate policy recommendations to Government which are actionable.*

*viii) Small and medium industries play a crucial role in spreading benefits of economic growth to the masses and are the ideal source for employment generation. They play a significant role in not only manufacturing per se but also in India's exports. They would require special focus and support to enhance their competitiveness.*

*ix) Public sector manufacturing industries would be another focus area for the Council keeping in view their pre-eminent role in manufacturing, particularly of capital goods. The public sector units*

*may be encouraged to develop business scales of global level based upon investment in technology and capacities.*

*x) Infrastructure development: Developing infrastructure particularly, Power, Ports and transportation is essential for the growth of manufacturing sector as well as India's overall economic growth.*

In the second Council Meeting, the draft Strategy paper prepared by the NMCC secretariat was placed for discussion and the members were requested to offer their suggestions and comments (including written comments) on it to enable preparation of the final paper. It was also acknowledged that in the preparation of the draft paper, inputs from Dr. Bibek Debroy, Dr. Surinder Kapur, and Members of the National Manufacturing Competitiveness Council have been used extensively by the NMCC. The highlights of draft Strategy paper is given below:

The draft Strategy paper outlines the Strategic directions for enhancing the Competitiveness of the Indian manufacturing sector. These steps are the start of a process, not the end. The paper details out the manufacturing imperative and enumerates tackling challenges facing Indian manufacturing along with certain strategy prescriptions. It also lays out the way forward covering further work in sub-sectors, managing implementation and creating monitoring mechanism.

### **Background**

- Since 1991, the ongoing progressive liberalization and globalization process have provided unprecedented opportunity for the growth and expansion of the Indian industry in general and the manufacturing sector in particular. Further to it, the Indian industry not only faces stiff competition from free imports but also continue its efforts to grow its export capability through competitiveness.
- Manufacturing sector which is a part of the industry accounts for about 17% in India's GDP with a share of 12% in total employment (48 million persons). More than 75% share in India's total exports comes from manufacturing sector. The manufacturing sector grew at an average of 6.3% during 1991 to 2003.
- India's share in the global trade is less than 1%, which is much below the potential. Five sectors viz gems and jewellery, textiles, engineering goods, chemicals, leather and leather goods account for 75% of the India's exports. The two trading blocks, US and EU, receive more than 50% of exports from India.
- In spite of manufacturing having been recognized as the vehicle for growth and emphasis placed on industry in several plan periods, it is a matter of concern that the contribution of manufacturing to GDP has remained below expectations.

- One of the major reasons for the low level of contribution has been our inability to build and maintain competitiveness needed to match global levels of competitiveness. The resultant low levels of such growth had their impact on employment generation.
- India with comparative advantage in labour, its past experience, large pool of skilled manpower, established raw material and supply base and growing domestic volumes has the potential to emerge as major manufacturing hub for the global market.
- Recognizing the importance of manufacturing in over-all economic growth of the country and in line with the priorities laid down in the National Common Minimum Programme, the United Progressive Alliance (UPA) Government has set up the National Manufacturing Competitiveness Council (NMCC), as an interdisciplinary and autonomous body at the highest level to serve as a policy forum for credible and coherent policy initiatives.
- The immediate task before NMCC, however, was to look into the total area of manufacturing activities in the context of increasing need for employment opportunities and to unlock the full potential of Indian Industry.
- To achieve these objectives, NMCC decided to pursue a two-pronged approach. First to prepare a National Manufacturing Strategy Paper to identify the areas of policy that are to be addressed and Second, proceed with detailed study and make recommendations in respect of sub-sectors of manufacturing that are assessed to have immediate potential for growth and employment.
- The challenges faced by Indian manufacturers raise important questions for both industry and government. While industry has to grapple with how best to maintain a competitive edge while operating in a globally competitive environment, the government has to dwell on how to create the conditions that foster not only a healthy & competitive manufacturing sector but also drive investments and growth.
- This calls for a breakthrough thinking on the part of all stakeholders as only bold growth targets may allow India to ride the next manufacturing wave.

## **Manufacturing imperative**

### **Importance of manufacturing to Indian economy**

- The 10<sup>th</sup> Five Year Plan (2002-07) projects an annual average real GDP growth of 8%. The government targets 7 to 8% growth over the next decade. While an average of 8% during the 10<sup>th</sup> Five Year Plan may now be impossible, there is no denying that a trend rate of 8% plus over the next decade and more is feasible.
- **Therefore, target growth rate for manufacturing has to be or at least 12 per cent as against the trend growth rate of 7 per cent achieved in last 10 years.**

- The solution to provide jobs to the millions (estimated that nearly 10 million people) joining the workforce can only be through a robust growth of manufacturing. Manufacturing growth would not only provide direct employment but also has a significant impact on employment creation in agriculture and services sectors, thus becoming the engine of both growth and employment.

## Competitiveness

- At a very broad level, some indications of competitiveness can be obtained from *World Competitiveness Reports*. More accurately, there are two such reports – *Global Competitiveness Report (GCR)*, published by World Economic Forum<sup>1</sup> and the *World Competitiveness Yearbook (WCY)*, published by International Institute for Management Development (IMD).
- While neither report is about manufacturing competitiveness alone, manufacturing does form an integral part of the rankings. What is pertinent is that companies compete. Countries or economies don't compete. However, government policies provide the environment within which companies compete.

## Components of manufacturing sector

- Of the 27% industrial contribution, around 9% is non-manufacturing industry (including mining and quarrying). The manufacturing contribution proper is around 18% of GDP. Manufacturing's share is a function not only of manufacturing growth, but also of growths in the other sectors.
- Even though historical trend shows that it has taken more than 20 years to increase the manufacturing share by five percentage points to around 18%, **there should be a game plan to increase manufacturing's share in GDP to something like 23% in 2015<sup>2</sup>.**
- An overall or aggregate target of 12% growth needs to be decomposed or disaggregated according to manufacturing sub-sectors. For instance, in the index of industrial production (IIP), there are 17 industry groups at the 2-digit level of classification.<sup>3</sup> This is indicated in the table below and is based on the National Industrial Classification (NIC).

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<sup>2</sup> The CII-McKinsey aspiration is 18-21% share of GDP by 2015.

<sup>3</sup> IIP only covers 80% of manufacturing.

NIC 2 -digit code	Description	Weight in IIP (%)	5 yr. Avg. growth (1999-2003)	Possible target growth (average)	Contribution to manufacturing growth (%) (Weight x Growth rate)
20-21	Food products	9.1	4.6	<b>7%</b>	.00637
22	Beverages, tobacco & related products	2.4	12.1	<b>10%</b>	.0024
23	Cotton textiles	5.5	0.3	<b>8%</b>	.0044
24	Wool, silk & man-made fibre textiles	2.3	6.4	<b>4%</b>	.00092
25	Jute & other vegetable fibre textiles (except cotton)	0.6	-0.4	<b>1%</b>	.00006
26	Textile products (including wearing apparel)	2.5	3.9	<b>17%</b>	.00425
27	Wood & wood products, furniture & fixtures	2.7	-7	<b>1%</b>	.00027
28	Paper & paper products & printing, publishing & allied industries	2.7	4.5	<b>10%</b>	.0027
29	Leather & leather & fur products	1.1	4.5	<b>8%</b>	.00088
30	Basic chemicals & chemical products (except petroleum & coal)	14.0	6.9	<b>18%</b>	.0252
31	Rubber, plastic, petroleum & coal	5.7	6.4	<b>7%</b>	.00399
32	Non-metallic mineral products	4.4	6.6	<b>7%</b>	.00308
33	Basic metal & alloy industries	7.5	5.9	<b>12%</b>	.009
34	Metal products & parts, except machinery & equipment	2.8	2.8	<b>7%</b>	.00196
35-36	Machinery & equipment, other than transport equipment	9.6	8.7	<b>20%</b>	.0192
37	Transport equipment & parts	4.0	8.4	<b>10%</b>	.004
38	Other manufacturing industries	2.6	2.5	<b>15%</b>	.0039
<b>Total</b>		<b>80.0<sup>4</sup></b>			<b>.09258</b>

<sup>4</sup> There are rounding approximations.

- One way of identifying sub-sectors for a thrust is in terms of possible employment generation. For instance, if one were to use this yardstick, one would probably pick codes 20-21 through 29 from the above list. The second way of identification of thrust areas is in terms of the weights that different sub-sectors have in overall manufacturing growth.
- **Based on the manufacturing sector performance in 2003-04 and 2004-05, the table above also shows aspirational growth targets for the 17 industry groups.** As the table shows, 10 per cent growth rate in manufacturing is within the realm of possibility and aspirational target of 12 per cent can be achieved by sustained implementation of various elements discussed in the following section of this paper.

## Tackling challenges facing Indian manufacturing

### Creating conditions for growth, investment & employment

- The growth of manufacturing sector is dependent to a large extent upon the role that the industry intends to play, given the role of the Government. Industry would need to invest in R&D and technology, need to have a continuing commitment to skills development & education, need to benchmark their performance against the best in class, need to adopt best manufacturing practices & production techniques, and need to deliver on globally acceptable quality levels.
- NSS survey held in 1999-2000<sup>5</sup> shows a labour force of 363.33 million and a workforce of 336.75 million, with an unemployment rate of 7.32%. In 2000, the total work force is estimated to be 397.88 million. Of this, 28.15 million, or 7.07% is in the organized sector<sup>6</sup>. The unorganized sector accounts for employment of 369.73 million, or 92.93%. While the average annual growth rate in employment was 2.89% between 1983 and 1987-88 and 2.50% between 1987-88 and 1993-94, it was 1.07% between 1993-94 and 1999-2000. If 10 million new jobs have to be created a year, manufacturing has a major role to play.
- Employment in manufacturing was 40.79 million in 1999-2000. Between 1993-94 and 1999-2000 the employment elasticity in manufacturing was 0.33 as compared to 0.59 between 1983 and 1987-88. If manufacturing grows at 9%, with an employment elasticity of 0.33, 1.2 million jobs are expected to be created in manufacturing a year. **If the employment elasticity were to increase to 0.59, 12% aspirational growth target means 2.9 million new jobs a year.** These are figures on direct job

<sup>5</sup> Large NSS surveys are roughly held at five-year intervals. Before 1999-2000, the last one was in 1993-94.

<sup>6</sup> *Economic Survey 2004-05* has an organized sector figure of 27 million in 2003, with a breakup of 18.6 million in the public sector and 8.4 million in the private sector.

creation. In addition, indirect jobs would be created as a result of multiplier effects<sup>7</sup>.

- It is therefore essential that a thorough review of the past policies which discouraged robust growth of manufacturing is undertaken and recommendations arrived at to rectify and improve conditions that not only encourage growth but also bring in investment and generate employment potential. **Towards this, the policy framework shall encourage building up scale of operations in the domestic market and also enable financial institutions finance global level projects.**
- **Large scale investment, both domestic and foreign would have to be attracted into the manufacturing sector to enable high-levels of growth envisaged. It is also essential that in order to be competitive, the manufacturing sector needs to be modernized through transfer of modern technologies. It is, in this context, a close interaction and coordination between the Investment Commission and the National Manufacturing Competitiveness Council becomes imperative. National Manufacturing Competitiveness Council would work towards achieving such coordination.**

## Targeting manufacturing & competitiveness

- Some of the constraints in pushing up manufacturing growth are generic in the sense that they cut across all manufacturing sectors. The others are more specific and pertain to specific sectors. However, the key component of any strategy is a means of measuring progress towards a defined goal. In this context, it is essential to understand international competitiveness, which is really a multi dimensional concept, dependent upon three main sets of factors - all taken together. viz.,
  - i) **Country specific advantages** - related to technological, financial and other infrastructural status of the economy vis-à-vis those of the highly developed economies where major competitors are located.
  - ii) **Industry specific advantage** - related to the type of industry where competitiveness is also affected by various fiscal and monetary policies which are changed from time to time.
  - iii) **Enterprise specific advantages** - related to a particular company, like the ability to acquire, assimilate, develop new technologies; capabilities to reduce production costs; cut down delivery cycles; enhance quality & productivity and after-sales-service etc.

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<sup>7</sup> Although CII-McKinsey suggest two to three times the direct figure.

## Driving cost competitiveness and domestic demand

- A number of recent studies have shown that India suffers on competitiveness due to various factors such as lack of scale of operations, lower operational efficiencies, higher transaction costs, higher incidence of indirect taxes, higher import duties, lower labour productivity, higher cost of capital, inadequate infrastructure, etc. One such study<sup>8</sup> points to the Chinese products being lower in cost by 30% in general in comparison to Indian products inspite of similar labour and other input costs. Further, Total Factor Productivity (TFP) comparisons establish that productivity of Indian manufacturing<sup>9</sup> is about one-fifth of US levels and about half the levels in Taiwan and South Korea.
- Indian manufacturing would be competitive only when the cost of manufacturing is low. Therefore, lowering cost of manufacture in India should be one of the prime focus areas to work upon in the council. Further, enhanced domestic demand can give rise to increased share of manufacturing in the economy. For stimulating domestic demand, while the focus could be on reducing indirect taxes and import duties, following generic heads need attention:

### Import duties

- Import duty head has several different strands. First, there is an argument that import duties need to be reduced. This argument is usually advanced when items imported are raw materials and intermediates and not finished goods.
- The Kelkar Task Force<sup>10</sup> recommended a four-tier import duty (that is, for manufactured goods) structure in 2006-07 – 5% for basic raw materials (coal, ores and concentrates, xylenes), 8% for intermediate goods (capital goods, basic chemicals, metals), 10% for finished goods other than consumer durables and 20% for consumer durables. **While the basic customs duty may be zero, imported products should face duties equivalent to domestic indirect taxes paid by domestic manufacturers.**

### Domestic indirect taxes

- Domestic indirect taxes are often singled out as a major reason why Indian manufacturing is uncompetitive. For instance, the CII-McKinsey report argues that total taxes on manufactured goods are 25 to 30% of the retail price in India, compared to 15% in China and indirect taxes contribute 50% to the difference in retail prices between India and China. Lower duties would have boosted the domestic market and permitted synergy (exploitation of economies of scale, attracting FDI) between domestic and export markets.

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<sup>8</sup> Learning from China to unlock India's manufacturing potential, CII-McKinsey Report, October 2002.

<sup>9</sup> Making Indian Manufacturing Globally Competitive, ACCENTURE

<sup>10</sup> *Report of the Task Force on Indirect Taxes*, Ministry of Finance and Company Affairs, December 2002.

- Reforming indirect taxes is also contingent on reforming direct taxes. In 2004-05, total tax revenue is 10.2% of GDP, if one includes Central taxes alone.<sup>11</sup> If one includes State and local level levies, the figure is more like 15%. Given expenditure commitments and demands on the government, this ratio probably needs to be 3% more as share of GDP. The Kelkar Task Force on implementation of the FRBM (Fiscal Responsibility and Budget Management) Act also argues that fiscal consolidation will primarily have to occur via the revenue route rather than the expenditure contraction route.<sup>12</sup>
- The broad shape of indirect tax reform is clear. **There should be a combined goods and service tax (GST), with service sector taxation integrated into the VAT framework instead of being a tax on turnover. This will be accompanied by a withdrawal of all other taxes like central excise, central sales tax, octroi, State-level sales tax, entry tax, stamp duties, transportation taxes and so on.**

### Export incentives/export subsidies

- With liberalization across the board, liberalization in selected enclaves (EOUs, SEZs and AEZs) has become somewhat irrelevant. If customs duties have come down and are going to drop further, what is the added attraction of these schemes, especially if there are going to be restrictions on sales in the domestic tariff area (DTA)? Quite often, debates about SEZs/AEZs vis-à-vis EOUs are about equal treatment in sales to the DTA and about concessional customs duties on such DTA sales. **With import duties declining, surely one could argue that there should be no restrictions on DTA sales. This might as well be completely freed up.**

### FDI and procedures

- Foreign investments mean both foreign portfolio investments and foreign direct investments (FDI). FDI brings better technology and management, access to marketing networks and offers competition, the latter helping Indian companies improve, quite apart from being good for consumers. This efficiency contribution of FDI is much more important. UNCTAD now has a FDI performance index ranking and a FDI potential index ranking. In 2002-03, India's FDI performance index ranking was 114<sup>th</sup> out of 140 countries.<sup>13</sup>
- There are procedural problems at all three levels of an enterprise are functioning – entry, functioning and exit, although foreign investors often tend to focus on the first. The expression transaction costs is sometimes used and such an expression also subsumes under it costs associated with inadequate infrastructure. A recent World Bank report benchmarks

<sup>11</sup> *Economic Survey 2004-05.*

<sup>12</sup> *Implementation of the Fiscal Responsibility and Budget Management Act, 2003, Report of the Task Force, July 2004.*

<sup>13</sup> *World Investment Report 2004, The Shift Towards Services, UNCTAD, 2004.*

India's transaction costs with some other countries in the world.<sup>14</sup> One should remember that **many, though not all, of these procedures are at the State government level where reform is necessary. Land, labour, water, electricity, environment are examples.**

### Interest rates

- High interest rates and availability of credit are often cited as problems. Whichever index one uses to measure inflation, annual inflation is around 6% now. With a PLR of 10.25%, this means a real rate of interest of 4.25%. In a capital scarce country, real interest rates will never be as low as global interest rates, although this is qualified by the harmonization that has taken place between global and domestic interest rates. Some parts of the Indian corporate sector are now allowed to borrow globally, though not all.

### Labour laws

- With the focus on creating an enabling environment that encourages new employment as a result of increased growth in various constituents of the manufacturing sector as well as skill development/ upgradation to enable such a growth to happen, a look at various labour related issues becomes essential.
- Labour law reform is usually equated with Chapter V-B of the Industrial Disputes Act (IDA), but the issues are more complicated. Subject to the caveat that labour is on the concurrent list of the Constitution, there are 45 Central Acts and 16 associated rules that deal directly with labour. There are others that indirectly deal with labour, like *the Boilers Act (1923)*, *the Collection of Statistics Act (1953)*, *the Dangerous Machines (Regulations) Act (1983)* and *the Emigration Act (1983)*. There is thus an issue of unification and harmonization. Reforming labour law has many dimensions and issues.
- **Given the other provisions of labour legislation, the requirement of governmental permission can be dispensed with, without adversely affecting the interests of labour.**
- **Competition cannot function without free exit. While a consensus on Chapter V-B is being arrived at, the need is for quick amendment of the other sections of IDA and implementation of other labour law reforms.**
- If the recommendations of the Second National Commission on Labour submitted in 2002 are **implemented, they will harmonize labour laws under five heads of industrial relations, wages, social security, safety and welfare and working conditions. While flexibility will improve in the organized labour market, there will simultaneously be better social security provisions in the unorganized one.**

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<sup>14</sup> *Doing Business in 2005*, World Bank, IFC and Oxford University Press.

## Investing in innovations & technology

- Investing in innovations is one of the pre-requisites to attain global competitiveness. Investing in R&D by the corporates and by the government of India to adopt technology ahead of markets is essential.
- The existing policies relating to R&D funding, incentives for supporting generic technologies, Engineering and physical sciences should be reviewed and steps taken to encourage better coordination of efforts and greater focus on innovation and productivity enhancing technologies.
- Prioritized support of advanced manufacturing technologies. The need for creating a coordination mechanism on Manufacturing Research and Development should be pursued.
- **Prototype development and design innovations would require to be supported. Creation of common testing facilities and centres of manufacturing technology excellence are essential. Management of these by the beneficiaries themselves would encourage the Indian manufacturing industry to invest in innovations, strengthen Patent and Trade Mark systems to encourage patenting and Trade Mark registrations.**
- In areas of critical importance, in addition to provision of certain tax relief measures on R&D expenditure by the industry, enhanced government funding of research & development activities becomes crucial to support the efforts of the manufacturing sector, especially if innovation and R&D is to form the basis of building comparative advantage.
- **This would call for sector wise study of technology status and building a future model for R&D support by the government, especially in the areas of emerging technologies which have the potential to transform products, processes and services.**
- **Specific needs of small businesses need to be attended to. Small Business innovation Research and Small Business technology transfer focusing on Manufacturing need to be addressed.**
- **The unique capabilities of the National Laboratories and the IITs and other Technical Institutions need to be leveraged to benefit the Small and Medium Manufacturing Industries.**

## Strengthening education & skill building

- For the Indian manufacturing to be globally competitive, it needs to attract the best brains. Towards this, **a close interaction is necessary between academia-industry-government for creating Centres of Excellence in manufacturing technologies.**

- **The quality of Technical education at the vocational level as well as the University level needs to be addressed. Special focus needs to be given to issues relating to the emerging requirements of Industry while designing the syllabus by these institutions.**
- If Indian manufacturing has to meet its aspirations, it will require producing 1.5 million technically skilled people every year in order to meet the incremental requirement of 20 million skilled technicians by 2015<sup>15</sup>.
- For delivering skills, the public sector driven initiative, through the Apprentices Act and ITIs (Industrial Training Institutes) has not been able to keep pace with changing requirements, and other forms of vocational training, through public-private partnerships, if not outright private sector provisioning, with training authorities delinked from certifying ones **OR the private sector should be encouraged to establish and operate demand driven technical training centres through financial and other incentives, under a carefully designed industry-managed, and government supported, quality control and accreditation system.**
- Any effort to improve human capital has to take into account the needs of not only the domestic market but also the increasing opportunities in the global market.

## Benchmarking against best practices & breakthrough thinking

- Adoption of global best practices in manufacturing is another area which requires attention for ensuring sustainable competitiveness. Benchmarking and standard setting has to begin from building the human resource and extended to the entire value chain. In this context, **NMCC would assist Industry associations in developing relevant sub-sector wise benchmark data bases that could help the industry measure itself against in the best in class performances. A Manufacturing Advisory Service could be established to deliver practical help to manufacturing SMEs.**
- A paradigm shift in manufacturing sector can be achieved, if manufacturing is not just viewed as a process in the factory, preceded by design and followed by sales but as a new way where R&D is as critical a component of product design to supply chain management and customer relations<sup>16</sup>. Conceptually, it is a movement from products to architecture (concept : classification based on the 'system' of production) where sector wise competitive advantages can be derived.
- **NMCC recommends setting up a group to study the concepts & applicability of manufacturing architecture<sup>17</sup> (integral vs modular) as relevant to the Indian conditions.**

<sup>15</sup> CII-McKinsey Report 'Made in India'

<sup>16</sup> Shoji Shiba, Professor emeritus of University of Tsukuba

<sup>17</sup> Prof. Takahiro Fujimoto, University of Tokyo

## Providing right market framework & regulatory environment

- Access to technology, larger investments that drive exploitation of economies of scale and scope, accessing market information and so on are in the private domain, although there is often a tendency to expect the government to provide or subsidize these efforts. But given fiscal and other limitations, there are constraints on what the government can effectively do. However, government would work towards providing the right market framework and regulatory environment that provides impetus to the manufacturing sector. In this endeavour, NMCC will provide appropriate policy recommendations to government that are actionable.
- The frame work would, need to ensure fair competition; better access to markets – both domestic and foreign; trade negotiations that ensure a level playing field for domestic manufacturers, review of existing regulations and reduce the burden of paperwork and inspector raj in respect of existing Laws, promote sub-sector wise policy on regulation and examine the issues relating to regulatory accountability.

## Enhancing the role of Small & Medium Enterprises (SMEs)

- The small scale sector has acquired a prominent place in the socio-economic development of the country during the last five decades. It plays a crucial role in spreading benefits of economic growth and employment generation, manufacturing export growth. Several problems associated with this sector prevent it from enabling further growth like access to timely & adequate credit, technological obsolescence, infrastructural bottlenecks, poor health of state financial corporations, and lack of R&D linkages, marketing constraints, disabling rules & regulations. The sector requires special focus and support to enhance its competitiveness.
- **One of the solutions for pushing manufacturing growth is through growth poles or industrial clusters, mentioned in the PURA (Provision of Urban Amenities in Rural Areas) context, in the 2005-06 budget speech.** While general taxation, interest rate or FDI policy problems will remain, it should be possible to have simplified procedures, including on labour laws, in these clusters. It should also be possible to have skill development and focused physical infrastructure initiatives. **The growth poles can cover all three elements of the cluster approach – industrial clusters, artisan clusters and agro-based clusters.**

While certain policy initiatives have been taken by the government in respect of SMEs in recent times, NMCC is separately examining the support needed to enable the sector face future challenges. A consultative process is already underway with concerned stakeholders.

## Enabling Public Sector Enterprises to meet competitive market conditions

- Given the type and range of problems faced by the country at the time of independence on the economic, social and strategic fronts, it became a pragmatic compulsion to use the public sector as an instrument for self-reliant growth and hence, Public Enterprises became central to India's philosophy of development.
- The dominant consideration for the continued large investments in public sector enterprises was to accelerate the growth of core sectors of economy ; to serve the equipment needs of strategically important sectors like Railways, Telecommunications, Nuclear Power, Defence, etc., and to provide a spring board for the economy to achieve a significant degree of self-sufficiency in the critical areas.
- However, keeping in view their pre-eminent role in manufacturing, particularly of capital goods, the National Manufacturing Competitiveness Council will study the reasons for the inadequate operational efficiency of the Public Sector and come up with suitable recommendations for improving their competitiveness, encouraging them to develop business scales of global level based on investments in technology and capacities.
- **Towards this NMCC would discuss with Department of Heavy Industry & Public Enterprises as well as Ministry of Defence various measures aimed at enhancing the competitiveness of the PSEs including further empowerment of various categories of CPSEs.**

## Infrastructure Development

- There can be no issue with the proposition that inadequate infrastructure renders Indian manufacturing uncompetitive. *Economic Survey 2004-05* lists power, telecom, posts, roads, ports (airports and seaports), civil aviation, railways, urban infrastructure and legal infrastructure as infrastructure.
- The issue is simply one of getting infrastructure reforms implemented and some areas of physical infrastructure are State subjects. From the manufacturing perspective, perhaps the most important infrastructure areas where reforms are to be speeded up are power, ports and railways, followed by roads.
- **Additional investments need to be made by the government in increasing the port capacities (over and above the currently planned expansions).**
- **Further, port operations & procedures need streamlining by simplifying the number of procedures, automating the processes, etc. with a view to bring down customs clearance time.**
- **While the Golden Quadrilateral (GQ) and the east-west and north-south corridor projects launched by the National Highways Authority of India**

**(NHAI) are steps in the right direction, port connectivity to manufacturing clusters and the GQ through targeted road development projects is essential.**

- **While the Electricity Act 2003 is a step in the right direction, state level power reform supported by rationalized regulatory framework needs to be put in place for enabling better access to quality power.**
- **The Cabinet Committee being serviced by the Planning Commission is fully seized of the matter and National Manufacturing Competitiveness Council would engage in discussing the specific infrastructure needs of manufacturing sector with Planning Commission periodically.**

## **Way forward**

- In order to be successful, Indian companies will need to adopt a global mid set to build scale and achieve cost excellence; acquire market access rapidly; strengthen design and innovation skills; build a global or regional operating foot print; and master the ability to manage a world-class talent pool and organization.
- These actions will form the foundations for ambitious growth and will need to be supported by a judicious choice of market segments and business models. In order to achieve this, 10 elements of the strategy have been identified which have been discussed in the previous section. An action plan for implementing these elements of the strategy would be prepared. This action plan would be subjected to rigorous monitoring and periodic review.
- Parallely, enable certain sectors that have the immediate potential for growth and employment, NMCC would continue to pursue a sub-sector wise engagement to identify impediments for growth and suggest initiatives aimed at enabling growth of the manufacturing sector. This engagement would also include specifying sub sector wise targets to be attained over a 10 year period. Certain sectors where such engagements have already taken place include :
  - Leather & Leather Goods
  - Food Processing
  - Textiles & Garments
  - Auto Components
  - Capital Goods
  - IT Hardware.

Others sectors engagement in the near future comprise –

- Paper
- Chemicals
- Pharmaceuticals
- Handicrafts & handlooms
- Gems & Jewellery, etc.

In addition SME segment and Public Sector Manufacturing Units would also be given due attention to enable them to evolve appropriate measures aimed at making them competitive.

## Managing implementation

In close association with the industry and academia, NMCC would formulate policies at three levels :

1. Country wide policies that are focused at reducing country costs and enhancing the transaction efficiency for business, including the necessary macroeconomic, regulatory and business environment, the physical infrastructure, and the educated and skilled labour under which manufacturing firms can invest and grow.
2. At sub-sectoral level, NMCC would work out strategic initiatives in priority segments, including trade policies, industrial transformation programmes, etc.
3. At the firm level, the NMCC would devise systems that should encourage increase of manufacturing capabilities in a non-discretionary manner, including adoption of total quality and productivity programmes, enabling technological upgrading and investment in plant and industrial skills, allowing a network of private sector led technical institutes & industrial extension services which are especially important for enabling SMEs to move up on high-skill needs.

## Creating a monitoring mechanism & measuring performance

- One of the weaknesses in achieving the goals set in the past has been weak implementation of policies and programmes. It is imperative that in order to achieve the high targets of growth and employment being aimed at, it is essential that the implementation mechanisms as well as institutions are properly designed. The National Manufacturing Competitiveness Council would work towards recommending creation of such mechanisms and institutions.
- NMCC will provide a platform with advice from government and industry to monitor the delivery by various stake holders on the recommendations/ action programme evolved for the manufacturing sector.
- Towards this end, a set of key performance indicators will be identified/ developed, which would allow a quantitative and qualitative assessment of the progress of manufacturing sector. These indicators shall allow monitoring of performance and effectiveness of initiatives/ actions by the government, industry and others supporting the manufacturing.

The third agenda item: the NMCC's Sub-sector Papers- Status report on interactions. The highlights of the 4<sup>th</sup> Agenda item are given below. The first Council meeting deliberated the identification of Sub-sectors for detailed study in the immediate future. The NMCC had prepared background notes in respect of eight sectors. The Council after deliberations had suggested the following:

- I. that the Council ought to form issue-based and sector-based working groups to interact with the Council; and
- II. that the Members of NMCC to send sector-specific papers for providing valuable insights and thoughts for initiating dialogue on important sectors identified during deliberations. Some papers could be targeted on generic issues.

As suggested, Sub-sector wise Groups were formed and first set of meetings was held in the NMCC in respect of the following sectors, viz.,

1. Leather and Leather Goods;
2. IT Hardware & Electronics;
3. Textiles & Garments;
4. Food Processing Industries;
5. Auto Components; and
6. Capital Goods Sector.

The NMCC also held a meeting on the generic issues of SMEs on Financing and Venture Capital. Further, the following Sub-group meetings were scheduled in April and May, 2005:

1. Paper Industry
2. Chemicals Industry
3. Human Resource requirements of Manufacturing Industry
4. Gems & Jewellery
5. Handlooms and Handicrafts
6. Pharmaceuticals

The following sub-sectors are also need to be studied in the near future:

1. Base metals
2. Cement
3. Fertilizers
4. Steel
5. Telecom equipment

Generic problems in respect of the following sub-sectors also are taken up paralelly:

1. Infrastructure for manufacturing
2. Innovation Policy
3. University industry and National laboratory coordination for strengthening manufacturing competitiveness

### Inputs/Notes From Members

The Council is grateful for the inputs(notes) received from the Members of the National Manufacturing Competitiveness Council which were discussed/ to be discussed in respective sub-groups:-

- a) Mr. Mukul Kasliwal- "Vision for growth of Indian Textiles sector" ;
- b) Mr. Yogesh Deveshwar - "Promotion on Forest and wood-based industry - A mega development multiplier";
- c) Mr. A.M. Naik - "Making Indian Capital Goods Competitive";
- d) Mr. Habil Khorakiwala "Nurturing R&D and Innovation - a must for India's long term manufacturing competitiveness";
- e) The President of CII - a note on "Upgradation of ITIs";
- f) Mr. Baba Kalyani - "Vision 2015 for the Indian Auto Component Industry (ACMA-McKinsey Report)"; and
- g) Dr. Surinder Kapur - "Break-through concepts to develop strategy for Manufacturing Sector in India".

This sector-wise note covers major aspects that emerged during each of the Sub-sector interactions. Some of the suggestions are generic while others are sector specific in nature. The on-going exercise of interactions will enable drawing up Sector- wise Strategy papers which are expected to provide more focused suggestions aimed at improving the overall competitiveness and growth prospects of each sub-sector. In addition to the above interactions, the NMCC also held consultations with Individual departmental heads to understand the issues relating to Textiles & Garments, Labour, Environment, Small Scale Industries, etc. A brief background and specific suggestions made in the respective Sub-group meetings is given below:

#### 1. Leather and Leather Goods :

The Subgroup meeting on Leather and Leather Goods sector was held on 25.1.2005. A copy of the minutes of this sub-group has already been circulated to the Members of the NMCC. NMCC is grateful to the background papers/presentations provided by: Dr. Amit Mitra, SG, FICCI; Dr. T. Ramaswami, Director, CLRI, and Mr. O.P. Kaul, President, Tata International Ltd.

Over the last five years, India's share of leather exports has remained around 2.3 percent while countries like China and Brazil are averaging around 18 percent and 3 percent respectively. Main threats to this sector are due to :

- huge wastage of Raw hides and skins of fallen animals
- lack of timely access to components and accessories
- rapid technological innovation
- WTO issues specifically Germany's concerns in connection with use of certain dyes and chemicals
- demand of specific packaging, etc.

There is a need for development of production systems to meet challenges of quality, efficiency, logistics, pollution etc. over the entire value chain; building market intelligence and range of products; emphasizing on managerial aspects; moving to higher return generating productions; production of standardized products; right-sizing of leather sector; mechanizing processes in the 2<sup>nd</sup> stage of production and technology upgradation/application for achieving increased competitiveness.

Specific suggestions:

- 1) There was a need to formulate schemes whereby recovery percentage of hides and skins of fallen animals is improved substantially not only to meet the projected demand but also to provide incomes and gainful employment to people from disadvantaged sections in the rural areas;
- 2) There was need to urgently implement the National Leather development Programme (NLDP) envisaged in the 10thPlan and to expand the programme with much larger investment for modernization in view of the potential available for export as well as in the domestic market. Cluster approach should be encouraged.
- 3) Design and development needs added emphasis and for this purpose funding is necessary. Technology development should be brought to the fore.
- 4) Transfer of technology, particularly those relating to environment should be encouraged.

- 5) In order to increase focus, mission mode should be adopted for achieving the targeted increase in production for both exports and domestic market and
- 6) The needs of Small Scale Units require further study and a meeting for this purpose would be separately called.

**Some key issues for deliberation:**

- a) The annual production value of Leather and leather goods is around US \$ 4 billion with annual exports US \$ 2 billion. The present target level for export by 2015 is US\$ 7 billion forming about 4% of the world trade in the sector. Given the potential for the sector, should we be aiming at 10% of the global trade?
- b) As the Leather & Leather Goods sector has not attracted major domestic players with global scales, what should be the approach for providing an attractive platform that would drive investments including foreign investment?
- c) How to enable the industry players become 'environment compliant' as this has been the single most factor effecting the growth in this segment?
- d) Government should place the Leather and Leather Goods industry (including footwear) on the same footing as Textiles/Garments in terms of direct and indirect taxation.
- e) In order to enable focused attention to this sub-sector, should Government adopt a mission mode?

**2. IT- Hardware and Electronics :**

The subgroup meeting on IT Hardware & Electronics Sector was held on 28.1.2005. A copy of the minutes of this sub-group has already been circulated to the Members of the NMCC. NMCC- is grateful to the background papers/presentations provided by: Dr. Amit Mitra, SG, FICCI ; Mr. Azim Premji, Chairman-WIPRO; Mr. Vinnie Mehta, Executive Director-MAIT and Dr. RC Chopra, Sr. Director, Ministry of IT. Secretary (IT) had spoken extensively regarding the need to support IT Hardware sector.

- The global production of electronic hardware in 2003 was US \$ 1430 billion of which the share of ICT and related components was more than 80%.

- While countries like China, South Korea, Taiwan and Malaysia have successfully captured a market share of US \$ 410 billion, India is producing/ assembling electronic hardware worth only US \$ 10 billion:
- As per the study carried out by MAIT-Ernst & Young, the demand in this sector could reach US \$ 73 billion by 2010.
- One of the reasons for China to have achieved a GDP share of 10% in electronic hardware is adoption of infrastructure status for this industry and following a differential VAT of 3-17%.
- The current employment of 1.5 million in this sector could be stepped up to 5.5 million by 2010 if the sector receives appropriate support.
- The main issue is the Zero duty regime in the context of the GOI signing the ITA-1 in 1997 which calls for elimination of customs duties on all 217 tariff lines covering around 800 products, including components, computer and telecom-related products by April 2005.

#### **Specific suggestions:**

- (i) Since the IT Hardware industry had not grown at a pace commensurate with its potential and the need of the country, it is necessary that corrective as well as promotive actions are taken expeditiously if the Industry were not to lose to import pressure;
- (ii) Penetration of PCs and other IT equipment in India was very low when compared with China and South East Asian countries. However, with increase use of IT, the situation could change with appropriate policies;
- (iii) The projected demand for hardware by 2010 is about US \$ 73 billion and if the domestic industry were to capture a substantial part of it, an additional four million jobs can be created.
- (iv) The existing tax structure requires revisiting in order to eliminate anomalies and to provide level playing field for the domestic industry; and
- (v) The whole gamut of policy initiatives suggested in the draft IT Hardware Policy would need to be considered and implemented expeditiously.

### Some key issues for deliberation:

- a) As India's PC penetration levels are just 14 per 1,000 people compare to global average of 30 per 1,000, what should be done to enhance PC penetration levels? Should special programmes as done in other countries be taken up; and
- b) What should be the approach to make IT Hardware industry competitive so that India emerges as an important global player not only in software but also in hardware?
- c) There is a doubt that growth in software development would be hampered if the hardware industry does not grow parallelly. This compels us to ensure speedy growth of manufacture of IT Hardware in India. , ,
- d) Extensive use of IT in promoting Indian Economy would become feasible when the cost of IT hardware, e.g., computers is within the reach of a larger population. This might require a national effort to make computers available at lower costs.
- e) Incentives/facilities that need to be provided for attracting investment in fab facilities in India.

### 3. Textiles and Garments:

The subgroup meeting Textiles and Garments sector was held on 12.2.2005. A copy of the minutes of this sub-group has already been circulated to the Members of the NMCC. NMCC is grateful to the background papers/presentations provided by: Mr. Vivek Bharati, Advisor-FICCI ; Sh. SP Oswal, Chairman, Vardhman Group; Mr. DL Sharma, Mahavir Spinning Mills Ltd. representing the CII Textiles Committee, and Mr. A. Saktivel, Chairman-AEPC. Shri Poornalingam, Secretary (Textiles) made the case for sorting out the issues relating to the sector expeditiously in view of its high potential for growth.

- Clothing is expected to grow at 9.6% CAGR compared to Textile, growth rate of 5.8% "CAGR and hence clothing could be the focus area.

- An examination of the status of Indian textile industry shows that "while in fibers/ yarns, we have the scale and acceptable quality levels, the same are lacking in weaving, processing, garmenting.
- Severe constraints are present in logistics/transportation.
- It is projected that India's exports are likely to grow from US \$ 14 bln. (Textiles: \$ 7.5' Bin. & Clothing \$ 6.5 bin.) to US \$ 50 bin. (Textiles: \$ 20 Bin. & Clothing \$ 30'bin.) provided certain reforms are carried out.
- While cotton cultivation needs to be a focus area in order to develop the yield, quality, etc. it is necessary to also focus on man made fibre (MMF) as larger opportunity exists in the synthetics.
- Global retailers will be looking towards countries that offer 'full package capabilities' and manufacturers with 'fabric to garment presence'.
- In terms of global market share, compared to India's share of 3.8%, China has a share of 28% which is the result of their policies related to flexible labour deployment, cheaper credit (as low as 3%) and adequate power & efficient infrastructure.

#### Specific suggestions:

- (i) Considering the potential that the sector offers, industry must think in terms of achieving a break-through rate of growth and come out with suggestions on what needs to be done by the government, the industry and the associations.
- (ii) There is a need for creating a level playing field between cotton and synthetics. Fiscal rationalization is necessary to place both cotton and polyester on the same footing.
- (iii) In terms of a road map for reaching US \$ 50 bin. Worth exports, the need is for focusing on higher end of the value chain, creation of global sized capacities across the value chain and strengthening the weak links in processing & weaving.
- (iv) Labour law reforms including increase in working. hours; modifications to Section 51-66 of The Factories Act, 1948 related to

employment of women between 7 p.m. and 6 a.m. as per; re-Look Chapter V-B of ID Act, 1947 as well as Section 10 of The Contract Labour (Regulation & Abolition) Act, 1970; amendment to the Factories Act (1948) to allow flexibility of working hours; clear exit policy route for entrepreneurs; grant of Income Tax benefits that enable 50% tax deduction in respect of profits from export of apparels ; mandatory working of customs clearance cells round the clock for 365 days a year; abolition of textile committee cells are some measures essential to realize future growth potential in this sector.

- (v) Any unit exporting 90% or more should be given same treatment as that of a unit in EOU/SEZ. Further, exporters to be allowed the EXIM Scrip route in lieu of all industry drawback.
- (vi) Import of plant & machinery is allowed at zero duty for a certain period.
- (vii) To meet the growing skill & manpower needs of the textile & garment sector, it is necessary that ITI's are enabled to include textile related training also.
- (viii) To enable quicker clearance of requisite recommendations on various labour related issues, it was felt that government could consider forming a 'Group of Ministers' (GOM).
- (ix) Consequent upon Sri Lanka and Bangladesh having successfully negotiated duty free access to the US markets in the post Tsunami scenario, there is an urgent need to focus on bilateral trade with US.

#### **Some key issues for deliberation:**

- a) As per the vision statement of Ministry of Textiles, the objective is to attain a level of 7% of global market. Should this be increased to 10%?
- b) To ensure the growth of the sector from US \$ 35 billion to US \$ 85 billion by 2010, what should be the measures to attract influx of huge Investments, technology upgradation and market access?
- f) As larger opportunity in future are expected lie in Man Made Fibre (MMF) segment, what steps are necessary to capitalize on the future demand potential ?; and

- g) Should a 'Mission mode' be adopted for ensuring that the suggested measures! action points are monitored for implementation?

#### 4. Food Processing Industries:

The subgroup meeting on Food Processing Industries was held on 25.2.2005. A copy of 'the minutes of this sub-group have already been circulated to the members of the NMCC. NMCC is grateful to the background papers/presentations provided by : Mr. P. Murari, Adviser to President, FICCI, Dr. Rajeev V. Dhar, Director of Indian Institute of Packaging, Dr. D.P. Singh, Secretary, Ministry of Food Processing Industries through his presentation, dealt with extensively on the issues relating to processing industry and had apprised the subgroup on the steps being taken by the Ministry in this regard.

There is an immediate need to resurrect the dormant food processing industry in the country as it has a multiplier effect on income generation, employment, etc. .

While the estimated total food market in 2003-04 stood at Rs.8,60,000crs., wastages account for nearly Rs. 50,000 crs. ' . In terms of Food processing growth, while agriculture & livestock 'recorded a CAGR of 3.7% between 93-94 and 2000-01, the manufacturing of food & beverages accounted for a CAGR of 7.1%. Food manufacturing has grown over 2.5 times faster than agriculture.

The absolute revenue increase in food manufacturing between 1993-2000 is significantly greater that that in IT and Pharmaceuticals. India accounts for only 1.3% of global agri exports. .

**Some of the identified impediments for lack of growth thus far are :**

- sector not being considered as a priority sector,
- non-availability of right quantity & quality of raw material, lack of effective demand,
- difficulty in complying with food laws, laxity on quality,
- high cost of processed foods (while tax on processed food is zero or marginal across the world, it is. nearly 30-40% in India);
- inefficient supply chain (Indian supply chain has 7-8 intermediaries,

- paucity of cold chain & retail chains); lack of suitable infrastructure;
- finance,
- Investment & credit issues;
- R&D and HRD issues.

#### Specific suggestions:

- (i) 'Farm to Fork concept' covering both safety and quality aspects needs to be adopted in the country.
- (ii) Further, there is a need to allow big retailers as they are the major drivers of processed food.
- (iii) There is a need to think in terms of contract farming & contract procurement and towards this, it was suggested that The Agriculture Procurement Act needs to be modified.
- (iv) Attention should be paid on harvesting technologies as there is a need to save on 25% wastages being incurred at present. Also there is a need to bring down the price differential between fresh and processed foods.
- (v) On food products, it was suggested that total tax incidence should not be more than 10% where excise should not exceed 8% and VAT should be at 4%.
- (vi) The sector may require Rs.60,000 in next 5 years and priority lending cap of Rs.5 cr. on P&M could be removed. Further, a food infrastructure bank with a Rs.1000 cr. seed capital could be established.
- (vii) Amendment to APMC Act may be necessary.

#### Some key issues for deliberation:

- a) In view of multiplicity of agencies (ministries/ departments) associated with administering 'Food Processing' segment, should a nodal authority be established for achieving a co-ordinated approach and implementation?; and

- b) What actions are required to attract foreign. and domestic investments in this sector? This seems to be an area where Technology and Capital Inputs are large and essential.

## 5. Auto Components :

The subgroup meeting on Auto Components sector was held on 15.3.2005. A copy of the minutes of this sub-group has already been circulated to the Members of the NMCC. NMCC is grateful to the background papers/presentations provided by : · M/s. McKinsey & Co. on behalf of ACMA, Mr. Deep Kapuria, President-ACMA, · Dr. Surinder Kapur, Member-NMCC.

- The domestic market is likely to grow at ~10% p.a over next 10 years but will lag behind China and small domestic market will impact on realizing export potential.
- A five fold growth potential exists - from current size of US \$ 6.7 billion (2004) to US \$ 33-40 billion (2015) comprising of US \$ 20-25 billion in exports and US \$ 13-15 in domestic consumption. The potential is only realizable if key barriers are removed.
- Global auto components market is expected to grow by 3% p.a to US \$ 1.65 trillion (2015) and the theoretically addressable market by India would be 42% or US \$ 700 billion.
- In terms of job creation, employment is expected to grow from 0.85 million (2003) to 3.25-3.95 million by 2015 comprising 0.9-1.15 million direct and balance indirect employment.
- Realizing the growth potential is dependent on an investment of US \$ 15 billion (2015) or US \$ 1.5 billion p.a. over next ten years and the industry at best can invest US \$ 0.5 billion p.a.

### Specific suggestions:

- (i) In spite of a five fold growth potential that exists for the auto components sector, commensurate investments of US \$ 1.5 billion p.a. may not materialize as the industry would only be in a position to chip in US \$ 0.5 billion p.a. Attracting FDI and new investments would be a major challenge that needs to be addressed.

- (ii) Availability of trained manpower to cater to the rising demand in this sector is expected to be a major hurdle. The Australian example could be studied.
- (iii) Without the creation of a strong demand in the domestic market, export realization may not fructify. For creating a strong domestic market, there is a need to adopt a country specific auto policy on the lines adopted by other countries like Japan, Brazil, Thailand, etc.
- (iv) Scale of operations cannot be achieved without a strong domestic demand and policies for increasing domestic demand should be considered.
- (v) Industry specific needs for operating out of SEZs/ SAPs would have to be worked out keeping in view the competition from Thailand arising out of the FTA recently signed and the sunset clause for EOUs.

**Some key issues for deliberation:**

- a) Realizing the growth potential of US\$ 40 billion by 2015 with an export level of US\$ 20. billion is dependent on a large infusion of investments into the sector. How to drive these investments?; and
- b) What measures are to be adopted to drive domestic demand in this segment which is key to increasing exports in the sector?
- c) How to meet the threat posed by FTA with Thailand?

**6. Capital Goods Sector:**

The subgroup meeting on Capital Goods sector was held on 16.3.2005. A copy of the minutes of this sub-group has already been circulated to the Members of the NMCC. Shri A.M. Naik, Member, NMCC gave a detailed note on making Indian Capital Goods industry competitive. Secretary, Defence Production gave detailed account of the issues relating to the participation of private sector in Defence Production and on the progress relating to offset principle.

- Over the last 4-5 decades, India had built up a good capital goods industry base and to a large extent met the needs for which such a base was set-up.
- The present need is to further build on the design & manufacturing capabilities established in the country.

- While certain organizations have been able to keep pace with technological changes and competitive pressures, a lot many have not kept pace for a variety of reasons.
- The present need is for re-defining the role of CG industry as future strategy in the sector would be driven by this definition. Further, to achieve long term domination, domestic CG industry needs nurturing.

#### Specific suggestions:

- (i) Capital goods manufacturing has the highest multiplier effect on employment and, therefore, policies that encourage growth and investment in Capital Goods Industry should be put in place.
- (ii) Rationalization of duty structure is essential in CG sector to create a level playing field with imports and public and private sectors. A two slab duty structure could be considered in place of current 0%/5%/10% structure.
- (iii) Inverted duty structure needs removal. In the context of zero duty regime, only a win-win model for the user-supplier will be acceptable.
- (iv) Provision of a technology upgradation fund on the lines of textiles upgradation fund could be considered, especially to upgrade the capabilities of SME segment.
- (v) IIP index related to Capital Goods needs re-examination in the context of inclusion of transportation requirement.
- (vi) Technology transfer to Indian CG sector must be made mandatory especially in the context of emerging new technologies/defence equipment imports while providing access to Indian markets. Also, technology could be leveraged through 'Offset' principle practiced by many countries.
- (vii) Domestic CG industry which is totally dependent upon imports of CRGO steel faces a problem as the world capacity has been blocked by China for its needs.
- (viii) Repatriation of earnings in project exports is not allowed till project completion certification is issued. This locks up earnings

from such projects and places additional financing burden on domestic CG industry.

- (ix) Infrastructure monitoring committee of the Prime Minister could consist of one or two representatives from private sector.
- (x) Establishment of a domestic ship building capability through JV route (public-private partnership) needs further exploration.
- (xi) Fiscal incentive of tax rebate of 150% on R&D expenses to be extended to domestic CG Sector,

**Some key issues for deliberation:**

- a) How to ensure a win-win situation for both the consuming sector and the domestic CG manufacturers in the context of zero duty regimes?
- b) What should be the policy level approach for ensuring that critical technologies required from outside the country by domestic CG industry continue to be available to enable them serve the domestic demand competitively?
- c) How to increase the role of private-public sector in the defence related manufacturing including leveraging the 'off-set' principle in defence procurement?
- d) Specifications and guidelines for procurement should encourage domestic CG manufacturers so that new technologies as well as new products are brought into the country.

**7. Small & Medium Enterprises:**

The subgroup meeting to look into the Financing and Venture Capital issues of SMEs was held on 4.2.2005. Secretary, SSI, elaborated on the issues relating to funding of the SSI and the actions needed to solve them urgently. A copy of the minutes of this sub-group has already been circulated to the Members of the NMCC. NMCC is grateful to the background papers/presentations provided by :- Ms. Uma Reddy, Member, NMCC; Mr. Gurbal Singh, DDG-CII ; Mr. VP Chopra, President-FASII, and Mr. Vivek Bharati, Adviser, and FICCI.

While the SSI sector grew at 8-10 percent during the last decade, the Tenth Plan target of 12 percent growth can only, is achieved if the sector is allowed to operate in a hassle free environment. This sector with 3.5 million SSI and a gross output pf Rs.7,42,021 crs. and 20 million employment is facing severe competition and lacks avenues for technology upgradation in addition to lack of access to adequate working capital which is given only on an incremental basis and not related to project specific requirements.

- With minimal credit flows to SSI sector, the problem is further compounded with the poor health of state financial institutions.
- One of the areas needing attention is the support for upgradation of technology for manufacturing, testing & packing in SSI sector.
- As most SSIs do not have R&D linkages, there is need to build strong institution and 8SI linkage.
- The Ministry is in an advanced stage of finalizing the Small and Medium Enterprise Development Bill (8MED) which inter-alia covers issues such as definition, registration, promotional measures, concept of how credit would be made available, harmonizing the inspection procedures, limited liability, etc.

#### **Specific suggestions:**

- (i) Banking Deptt./sector representatives were to bring out specific requirements from SSI Ministry/ SSI Associations in order to create a mechanism that would enable the Banks to lend more freely to SSIs;
- (ii) Examination of issues relating to making SIDBI more effective instrument in providing finance to SMEs (SSIs) ;
- (iii) Review the lending by banking institutions to small scale sector including the working of 'Credit Guarantee Fund Trust;
- (iv) Examination of issues of technology upgradation and common test centers;
- (v) venture capital funding ;
- (vi) Request for suggestions of RBI for improving the lending.

#### **Some key issues for deliberation:**

- a) How to improve the lending to SME sector and also ensure that venture capital funds flow to this segment.
- c) How to address the issue of competitiveness of SMEs in the wake of import competition?

The fourth agenda item of the Council meeting was the NMCC's Manufacturing Competitiveness Programme announced in the Budget 2005-06 - Status report. The following are the highlights of the 4<sup>th</sup> Agenda item:

The progressive liberalization of peak tariff rates by Government during the recent years would have had some positive as well as some negative impacts on the domestic industry. A recent study by ICRIER regarding such impact brings out that there would be winners and losers when the average peak tariff rates are brought down from 20% to about 10% to be in line with the tariffs in the South East Asian countries. Needless to say that those industries which are hit by the import competition need to be provided some assistance in restructuring so that the cost of adjustment to import competition is kept low and the industry is able to meet the challenge of competition. This issue was raised by Chairman, NMCC with the Finance Minister in February, 2005.

The Finance Minister in his budget speech while acknowledging the important role to be played by the manufacturing sector, has announced a scheme called the "Manufacturing Competitiveness Programme." He said,

*"Worldwide, it is manufacturing that has driven growth. In order to revive the manufacturing sector, particularly small and medium enterprises, and to enable them to adjust to the competitive pressures caused by liberalization and moderation of tariff rates, I propose to launch a new scheme that will help them strengthen their operations and sharpen their competitiveness. The scheme will be called the "Manufacturing Competitiveness Programme". The design of the scheme will be worked out by the National Manufacturing Competitiveness Council in consultation with the industry."*

The Chairman, NMCC took a preliminary meeting on 1.4.05 to discuss the design of a scheme which will help to sharpen the competitiveness of Indian Industry particularly those in the SME sector. Secretary (SSI), DC (SSI), Chairman, SIDBI, DG (CII), SG (FICCI), representative of ASSOCHAM, Dr. Surinder Kapur, Member, NMCC and Ms. Uma Reddy, Member, NMCC participated in the discussion. Chairman, NMCC mentioned about a program operating in USA for enabling firms to meet challenge of import competition. The elements of that programme include assistance to firms affected by import competition through part funding of their restructuring efforts. It provides matching funds towards

cost of consultants, experts, designers, etc., for studies aimed at improvements in competitiveness of a particular industry. The projects could be in areas such as manufacturing, engineering, marketing, information technology and quality. A brief note on that programme is at **Annex-II**. This programme as well as other ideas for improving competitiveness of the SMEs was discussed at the meeting.

It was generally felt that the scheme evolved by USA gives a useful insight and is a good model to help Small and Medium Industries in meeting the challenge of import competition. It was felt by the participants of the meeting held on 1<sup>st</sup> April, 2005 that a similar scheme might help in undertaking a diagnostic study for restructuring their industries and to meet import competition in a globalizing scenario. Several other ideas were also mentioned during the discussions in assisting small and medium industry either individually or in a cluster in their preparation of restructuring package. The experience from the initiatives now being pursued by Government and the industry would need to be studied together with the possibilities of pooling different schemes that are in existence. Pursuing the idea of cluster development as a means to improve competitiveness also needs urgent examination.

It was felt that while designing the scheme, the important elements that would require attention are:

- (i) the scheme should be simple and flexible;
- (ii) criteria for providing the assistance should be clearly spelt out;
- (iii) the agency that will disburse the assistance should be identified;
- (iv) the institutional mechanism for administering the scheme, including handholding operations during the period of operation of the scheme should be worked out; and
- (v) it should be ensured that the scheme would be WTO compatible.

It was decided that a small group consisting of Member-Secretary, NMCC, Secretary (SSI) and representatives from industry associations and Dr. Surinder Kapur, Member, NMCC would work out the scheme details in about six weeks time.

## Following Points were made by the Council Members:

### On Competitiveness and Employment

Mr. Ratan Tata mentioned that it is a dilemma that the NMCC faces. He cited the example of textiles & garments, where cotton pricing has made it more expensive in India than elsewhere and the effect of labour laws which have made spinning & weaving more expensive. He felt that one could perhaps identify those industries that can be made healthy but not competitive for reasons of employment. He advocated focus on those industries where comparative advantage is present in terms of abundant raw material base, or the markets that can provide scale, or industries which have high content of skill & intellectual inputs. We could then, perhaps, attempt could be made to identify thrust areas. He was of the opinion that there is a need to bifurcate the approach in terms of how to make some industries competitive in the Indian context and then make some of our industries globally competitive.

Dr.(Mrs.) Isher Judge Ahluwalia observed that it should be clearly brought out that in some cases, competitiveness may not necessarily result in employment generation but in other cases, gaining competitiveness will generate growth and through scale effect there would be much more output generation and this in-turn would generate employment.

Chairman, NMCC recalled that the Employment aspect was also raised in the first meeting of the NMCC and certain clarity was also brought out in the matter by the Hon'ble Prime Minister. He observed that the underlying idea of making the manufacturing sector competitive is to enable it to grow faster. He felt that any effort to improve the competitiveness is bound to impact the cost of manufacture and this in turn could drive the demand which could result in additional employment generation.

According to Chairman, improved competitiveness would result in a larger share of the global market. He opined that competitiveness and employment are not contradictory. According to him, one of the reasons for focusing on certain sub-sectors like Textiles & Garments, Leather & Leather Goods, Handicrafts, Food processing, etc. was because of their employment potential. He welcomed the opinion of the council members on the subject matter as, in his opinion, increased Competitiveness of the Indian Economy will generate large employment.

Mr. V Govindarajan, pointed out that the draft Strategy paper elaborates on Competitiveness. He further added that in the context of the sub-sectors, the Agenda item no.3 specifically states the sectors covered thus far and those expected to be covered in the immediate future. He welcomed ideas from the Council members in prioritizing the same.

Mr. Y C Deveshwar, opined that we cannot move away from the fact that 10 million people who come into the job market every year must be given employment. He recalled the Hon'ble Prime Minister's observation that if industries associated with any thing that is linked to the land and any thing that is produced from the land are made competitive then we have the best chance of being able to get the growth as well as ensure employment.

He felt that industries associated with agro processing, rubber, textiles, paper, food processing , poultry, herbal based, leather, cotton, fisheries, etc. are best examples of focus areas for prioritization. He observed that competitiveness is absolutely essential and the Council must not loose focus on this.

Prof. Sekhar Choudhuri felt that as discussed in the first meeting, the subject of competitiveness may not go along with employment generation. He expressed that those industries which are contemplating to achieve global competitiveness may not be in a position to effectively contribute to employment generation. He felt that there may be other industries in the value chain which are more amenable for creating more employment.

Mr. V Govindarajan, Member Secretary, NMCC while summing up the deliberations on Agenda item no.1 observed that no reservation in the context of SMEs is being proposed by NMCC. He further observed that given the fact that SMEs are present in the Indian context, their competitiveness is equally important if the overall competitiveness of the industry is to be improved. It is in this context that the Council needs to consider measures related to SMEs. He brought to the attention of the members that the Agenda item no.4 brings out a suggested scheme in the context of SMEs.

## The National Strategy for Manufacturing(NSM)

While initiating discussions on Agenda item no.2, Member Secretary, observed that it is a draft discussion paper prepared with inputs from Prof. Bibek Debroy and a concise Strategy paper would subsequently be drawn up as a result of the ensuing discussions. He informed the Council that the aspect of engaging State governments also needs to be considered before drawing up the Strategy paper as they have a large role to play in increasing the competitiveness. He urged the council to deliberate on the 12 per cent growth target for manufacturing indicated in the draft paper. He also requested the Council to decide on whether to have manufacturing's contribution to GDP as a target or just a growth rate for manufacturing sector as a target. He also sought the opinion of the council on having sub-sector wise growth targets. He then welcomed the Council to deliberate on Strategy paper, 'The National Strategy for Manufacturing- A discussion paper'.

Prof. Bibek Debroy drew the attention of the Council members in establishing certain targets that are doable and feasible. He also expressed that the Strategy paper should list out constraints (generic & cutting across all sectors) that need to be eased out in attainment of laid down targets. He felt that a target based on share of GDP cannot be considered in isolation as it is also dependent upon how the other sectors like services perform.

He observed that the thrust of argument in the discussion paper is based on the premise of a growth target for manufacturing. Three scenarios were considered and a more reasonable target of 12 percent growth has been indicated. He was of the opinion that 12 percent growth in manufacturing supported by the trend growth rates in agriculture and services could result in a GDP growth of 8 per cent. Further, if the elasticity of employment in manufacturing were to go back to the levels prevailing in 80s, then the 12 percent growth in manufacturing could translate into 2.9 million additional jobs per annum. It was also mentioned that at the 2 digit level (as per IIP classification), certain targets have been indicated for the 17 sub-sectors of manufacturing. He felt that the bulk of the paper is about generic constraints like indirect taxes, infrastructure etc. with suggestions of corrective actions needed.

Mr. Ratan Tata, expressed that the Council must identify certain thrust areas where we can build a global presence. He cited the example

of China which had planned for global dominance in certain areas, be it in steel or textiles & garments, or consumer products, etc. He advocated the need for the council to identify few areas for global dominance and in this context, inherent comparative advantages like domestic availability of raw material, presence of large domestic market for enabling scale of operations, availability of certain specific skill sets should be considered.

Mr. Ratan Tata, felt that an image appears to have got formed that small scale industry is a feeder industry for the large scale industry and is an employment generator. He advocated that small scale must be seen as a breeding ground for technology and cited the example of USA where small companies have been the source of technology even for larger companies. He advocated the need for redefining the operating sphere of small scale industries and viewing them as generators of innovation & technology.

Dr.(Mrs.) Isher Judge Ahluwalia, observed that the paper would have to be more Strategic in content and more focused. As drafted the Strategy paper may look “more of the same” and has not identified any break-through projects. She felt that a 15 per cent growth target in manufacturing is attainable but was of the opinion that the NMCC should re-consider the idea of putting a growth target in the strategy paper. According to her, if the council agrees on certain thrust areas, then it is very important to spell out their forward and backward linkages with other sectors as this would enable addressing larger issues of livelihood, employment, etc. She cited the example of food processing where among other things, target achievement is also dependent upon agricultural reforms and employment in the sector could come from its backward linkages. She felt that achieving incremental improvements in various sub-sectors while contributing to growth in manufacturing may not result in quantum jumps which are needed.

While appreciating the need for suitable support and incentives to small scale sector, she expressed that the council must approach the question of scale much more integrally. In respect of public sector enterprises, she felt that there is a need for the council to comment on aspects like restructuring, exit, etc. It was also suggested that the ranking of states for business should form a part of the strategy paper.

Mr. Y.C. Deweshwar pointed out that any growth per se in manufacturing would definitely have an impact on growth in both

agriculture and services sectors. He suggested that just like the role played by audit firms, the formation of similar institutions or firms of reputation specially in the area of environment & safety to carry out certifications related to environment should be considered. He further pointed out that rather than defining 'dominance' on the basis of some Indian situation, it should be defined in the global context, keeping in mind the 'Competition Law'.

Mr. Suresh Neotia while supporting Mr. YC Deveshwar's idea on audit firms in the area of environment & safety expressed that in reality the time taken for a project to be put into implementation mode is still very large because of uncertainties associated with environment clearances. He felt that this aspect needs attention if investment is to become a reality in quick time.

Dr. RA Mashelkar felt that deep concerns still exist on environment issues and cited the recombinant pharma example and expressed that there is a need for a dialogue process between concerned parties to resolve issues.

Mr. Jamshyd N. Godrej, while agreeing to the general approach enunciated in the discussion paper on growth in manufacturing, opined that there should be a method of prioritizing the listed constraints as he felt that some of the constraints could demand immediate attention. He cited the example of impending constraint in ports capacity and stated that if one goes by the NASCOM report on demand supply gaps in IT sector for engineering students, there could be void in meeting the demand for engineers in manufacturing sector.

Mr. Anwarul Hoda, observed that while the draft paper is an excellent summary of all the constraints bedeviling Indian manufacturing sector, some of the suggestions made in the paper need to be developed further. He felt that 12 percent growth target for manufacturing was appropriate. While commenting on various issues identified in the discussion paper, he felt that NMCC must express its own view in respect of the pattern (slabs) of import duties in future. He expressed that if uniform duties cannot be achieved then there should be tariff compression and at the least, tariff dispersion. With reference to the mention of proposals made to WTO, he stated that in reality, the proposals with WTO do not have the inevitability as is being made out in

the discussion paper. In respect of FTA, he felt that main issue with India's FTA with Thailand was the agreement on 'early harvest scheme' , where by duties on some products were to be reduced to zero within a short span of time without ensuring that the duties on inputs for such items are also reduced to zero and cited the case of television sets from Thailand. He suggested that much can be achieved in FTA's, if the duties on industrial products are comprehensively brought down within the agreed time periods rather than deciding of move towards a zero duty structure. Commenting on the domestic indirect taxes, he felt that while Kelkar committee has recommended a maximum of 20 per cent covering both state & central level taxes, NMCC should give its own recommendation on the subject.

On the subject of export incentives and export subsidies, he expressed that our exports must be made tax neutral and WTO not only allows it but has also laid down guidelines on the manner in which such exemption & rebating is to be carried out. In respect of DTA sales from SEZs, he implored the members to consider the relevance of SEZ strategy as duties are expected to come down. He opined that since the need is for world class infrastructure, the concept of economic regions could be considered where there may be no fiscal benefit but world class infrastructure could be provided. He urged NMCC to take a view on the matter related to freeing up restrictions on DTA sales.

On the issue of FDI and procedures, he felt that while barriers at the central level are gone in respect of manufacturing sector, he enquired if environment concerns are becoming a big constraint in the form of delays and increased inspections. He felt that issues related to the subject of Contract Labour (Regulation and Abolition) Act need more elaboration in the draft discussion paper and desired to know from the members of NMCC if this act is impacting SMEs also.

On strengthening education & skill building, he felt that NMCC must recommend what is the best way of proceeding in the matter of private & public partnership. On the subject of clusters, he opined that Planning Commission's view in the matter of small & medium enterprises is to encourage development of parks, etc. but they should be managed by the industry itself and not by the government.

Dr. R.A. Mashelkar, recalled Prime Minister's advice to the Council to think big. In the context of technology, he felt that in addition to the emphasis on technology development, the current business realities may call for technology acquisition as an alternate strategy. He advocated setting up a 'Global Technology Acquisition Fund' and urged the members to suggest ways of designing an appropriate scheme that could help Indian industry to acquire very highly technology intensive companies abroad when ever such opportunities arise. On the subject of education, he opined that in the self interest of the industry, private sector has to step in and in the context of skills development, he felt that the council must make bold recommendations with the active participation of private sector. Mr. Anwarul Hoda while endorsing the suggestion made by Dr RA Mashelkar on the setting up a 'Global Technology Acquisition Fund' opined that the approach followed by the European Union in assisting AIRBUS could be studied. He also cited the example of support to extended to Boeing in USA.

Mr. Vivek Bharti, pointed out that growth in agriculture & allied sectors must be factored into the Strategy paper and felt that agri sector reforms and expansion of rural markets would need emphasis especially in the context of expansion of home markets. He suggested that the importance of retailing should also be brought out as they deal with sale of manufactured products. He felt that industry associations could play an important role in enabling certain States to improve their prospects for attracting FDI. Further, on skills & development, he felt that the larger issue of deregulation in the education sector could be looked at. On infrastructure, he felt that benchmark data on cost & quality of our infrastructure should be clearly brought out especially in comparison with some of the Asian neighbors. He suggested that industry associations could not only partner NMCC in the benchmarking exercise but also in carrying out other base line surveys.

Mr. Priyadarshi Thakur, felt that adoption of the target growth rate of 12 percent in manufacturing would be dependent upon its contribution to the GDP growth as well as the consequent employment generation potential that may come about on account of growth in certain sectors. He was of the opinion that the private sector would need to play a large role in the attainment of the manufacturing growth target and suggested that the NMCC in its advisory capacity could recommend the role that public sector is expected to play in future.

He felt that even in cases where a sub-sector may have low employment potential but better chances of attaining increased global market share, such sectors would need to be encouraged. In terms of backward and forward linkages for employment, he felt that auto sector would be an ideal example. While looking at the competitiveness of the manufacturing sector, he opined that the Council should not lose sight of the contribution made by public sector enterprises. He expressed a word of caution while dealing with the subject of education, as one was not dealing with the education policy per se but in its limited context of manufacturing competitiveness.

Dr. Surinder Kapur, observed that in the context of thinking big, certain countries like USA, Japan, etc. succeeded when they had set themselves certain overreaching goals for attainment like 'putting a man on the moon' and 'becoming a centre for semi-conductors'. He opined that the council must suggest certain break-through projects in different sub-sectors which could make a bold difference in the manufacturing sector growth in future.

In the context of achieving global dominance, Prof. Shekhar Chaudhuri opined that the NMCC could consider identifying certain firms for selective support by the government. Such support could be considered for an industry segment rather than championing the cause for an individual firm. Mr. Ratan Tata cited the example of MITI's approach in Japan in automotive and semi-conductor areas as well as approach followed in USA for defence contracts where certain firms are identified and supported. Mr. Vivek Bharati felt that it is necessary to identify the instruments of support in such cases and cited the examples of provision of long term capital and exemptions as such instruments.

Chairman, observed that useful suggestions have emerged and it would be the intent of the NMCC secretariat to bring out the second version of the Strategy paper by the next meeting of the council. He also expressed those individual consultations with the council members on the strategy paper would be carried out and felt that depending upon particular issues, NMCC could take a firm stand vide its recommendations. He commented the suggestions of Mr. Ratan Tata and Dr. Isher Judge Ahluwalia and requested them and other members to suggest the thrust areas. He also enquired about the process to be followed in this context before the next meeting of the council.

## On Sub-Sectors

Chairman, NMCC informed the Council that Agenda item no.3 brings out the summary of interactions held with various Sub-sector representatives till date. He said, the NMCC recounted the efforts made till date in the dialogue with various Sub-groups and industry associations. This has helped in not only identifying the road blocks but also looking at both generic issues cutting across various sub-sectors and specific issues related to each sub-sector with a view to evolving corrective actions. He felt that the entire exercise is oriented towards bringing about a sustained economic growth of 8% and enabling a better standard of living for people at large.

Dr. R.A. Mashelkar recalled that of the 12 sub-sectors identified, some of them require immediate attention and some of them are self starters and quoted the example of Drugs & Pharmaceuticals where several initiative have already been taken to enhance their global competitiveness. In the context of employment generation, he cited the example of clinical research where the potential for women to get employed is huge. He felt that the council should concentrate on identifying certain immediate measures needed to enable other sector's attain global competitiveness.

Mr. Mukul Kasliwal felt that the council is addressing a sector like textiles where we are naturally globally competitive. He expressed that this sector with a right combination of corrective measures can yield not only competitiveness but also employment. He felt that the council should think of a time horizon of 10-15 years and areas where we have natural competitive advantage should be leveraged. He expressed that the recently announced policy of allowing women to work 24 hr. shifts is a step in the right direction for the textile & garment industry.

Mr. Habil Khorakhiwala suggested that strategies must be evolved around our strengths and felt that the Council must concentrate on removing the road blocks in enabling identified sectors attain competitiveness. He felt that the areas which need active support are innovation and R&D.

Mr. Anupam Dasgupta, expressed that in respect Agenda item no. 1, the council must take note of the Kelkar Committee recommendations in defence sector where some good suggestions have been made

particularly in respect of SMEs and what they can contribute to the defence sector.

Mr. Suresh Neotia, observed that in respect of Skill Development and public-private partnership, employability is the most important factor that needs attention. He cited the example of construction industry. He urged the Council to recommend a structure of public-private partnership that can give a push to employability.

Ms. Uma Reddy, opined that SSI sector cuts across all sectors and has core competency in manufacture. She recalled the sub-committee discussions on the need for stronger emphasis on linkages between large industry and the SSI sector and felt that we have moved away from the concept of sub-contracting to outsourcing. She observed that SSI sector is not looking for reservation but an enabling environment that encourage development of competitiveness.

The NMCC agreed to Chairman's suggestion that over the next few months, interactions with other identified Sub-sectors could be completed and then Sub-sector wise strategy papers could be placed before the Council for deliberations.

### **Manufacturing Competitiveness Programme**

Chairman informed the council that Agenda item no.4 relates to the 'Manufacturing Competitiveness Programme' scheme announced by the Finance Minister in his budget speech where in it was suggested that the NMCC would work out the modalities of the scheme. He sought the opinion and suggestions from the council members.

Mr. V Govindarajan, briefly outlined the contents of Agenda item no.4 on enabling small & medium industry meet import competition. In this regard, the methodology followed in respect of assistance towards SME sector by the US government was mentioned. He also brought to the attention of the Council members that a meeting on the subject was held on 1<sup>st</sup> April under the Chairmanship of Dr. V Krishnamurthy, where Secretary, SSI & AR and some members of the NMCC had participated. It was decided that a small group would prepare a base paper which could be considered by the Council before submission to the government.

Mr. Jamshyd N. Godrej, opined that anomalies perhaps hurt small enterprises more than the large ones. He offered to submit the scheme prevalent in UK for supporting innovation & technology upgrade in SME sector. Chairman suggested that the US scheme enclosed with the paper could be studied in detail by the members and suggestions offered on specific proposals.

Mr. YC Deveshwar, pointed out that in the context of role of small scale, branding and marketing are issues needing attention. Ms. Uma Reddy, felt that the proposed scheme should also talk about technology upgradation. Mr. Anupam Dasgupta mentioned that the schemes existing as on date in SME sector would need review as discussed in the first meeting.

While summing up the discussion on the Agenda item no.4, Mr. V Govindarajan observed that all aspects & existing schemes would be considered in addition to the USA example circulated as part of the agenda. Mr. Surinder Kapur observed that the focus must be on defining what competitiveness means to SME sector and cited the example of TQM initiative of CII.

### **In Conclusion**

Chairman while concluding, stated that there is a continuing dialogue with the Finance Ministry and he has the assurance from the Finance Ministry as well as the Finance Minister that as and when the NMCC comes up with suitable recommendations, the same would be considered. He also expressed that certain FTA related issues have been brought to the attention of the Prime Minister and hoped that there would be wider consultations before entering into further FTAs. He also mentioned about the dialogue with the Ministry of Environment and initial discussions with the Labour Ministry as well as certain trade unions and expected that further dialogue would be continued. It was also mentioned that the issue of implementation of NMCC recommendations in a 'Mission mode' in Textiles and Leather has been taken up with the government. Further, he recalled Prime Minister's observation that the NMCC is a unique Council with important linkages with Investment Commission, NAC, etc. and that any suggestion coming out of the Council would be viewed seriously for implementation. He thanked all the members for their active participation in the deliberations.

## **Highlights of the Budget, 2005-06 announcements made in respect of some of the sectors relating to manufacturing:**

### **Textiles & Handlooms**

- Creation of Technology Upgradation Fund for Textiles Sector with a provision of Rs.435 Crore.
- Introduction of 10 per cent capital subsidy scheme for the textile processing sector in addition to the normal benefits available under the TUF Scheme.
- The Ministry of Textiles to take up 20 clusters in the first phase at a cost of Rs.40 crore.
- The Government is implementing a life insurance scheme for handloom weavers which provide insurance cover up to Rs.50,000 to cover 20 lakh weavers in 2 years and will cost Rs.30 crore per year when fully rolled out. The Government is also implementing a health insurance package for weavers to cover 2 lakh weavers at a recurring cost of Rs.30 crore per year.
- For most textile machinery, FM proposes to reduce the duty from 20 per cent to 10 per cent, in order to help the textile industry acquire a competitive edge in the post-quota regime.
- Keeping in mind the crucial need to encourage the textile sector, the customs duty rates on polyester and nylon chips, textile fibres, yarns and intermediates, fabrics, and garments have been proposed to be reduced from 20 per cent to 15 per cent.
- Like last, year, FM to prepare the textile industry to meet the challenges of the post-quota regime, he re-affirmed that the CENVAT exemption route for natural fibres will remain in force. He also proposed to give independent texturizers the option to avail of the exemption route or pay 8 per cent excise duty with CENVAT credit.

### **Pharma & Bio-technology**

- Proposal to enhance the corpus fund of Rs.150 crore set up for supporting research and development in pharma and bio-technology sector in phases beginning next year. This will enable realizing the potential of the country to become an attractive destination for outsourcing in drug discovery and clinical research, and for co-development of drugs and manufacturing. In bio-technology, the industry has the potential to be a global leader supplying novel technologies and products to the health and agriculture sectors.

- Pharmaceuticals and biotechnology are sunrise sectors. FM proposes to reduce the customs duty on nine specified machinery used in these two sectors to 5 per cent.

## Small Scale Industries

- De-reservation (from SSI Reserved list) of 30 items in the category of 'textile products, including hosiery', to give impetus for rapid growth of the sector.
- The capital subsidy scheme, and a provision of Rs.135 crore were made for "Promotion of SSI Schemes". That provision is being enhanced to Rs.173 crore in 2005-06. Small Industries Development Bank of India (SIDBI) has established this year a SME Growth Fund with a corpus of Rs.500 crore. Small and medium units in knowledge-based industries such as pharma, biotech, and IT will be provided equity support through this fund.
- Proposal to introduce in this session the Small and Medium Enterprises Development Bill.
- It has been proposed to raise the ceiling for SSI exemption based on turnover from the level of Rs.3 crore per year to Rs.4 crore per year. Further, SSI units will now have only two options: either full exemption on the first clearance of Rs.1 crore or normal duty on the first clearance of Rs. 1 crore with CENVAT credit.

## Food Processing

- The food processing industry is growing at a rate which generates 2.5 lakh jobs every year. To encourage the food processing industry, he proposes to reduce the duty on refrigerated vans from 20 per cent to 10 per cent.

## Skill Training

- Skills development, especially for youth who have only minimal formal education, is an area which can no longer be ignored. Last July, a programme to upgrade 500 Industrial Training Institutes (ITIs) was announced. In the current year 100 ITIs have been identified. Out of them 67 ITIs in 15 States/Union Territories have been linked with industry and will be upgraded at a cost of Rs.1.6 crore each.
- There is a demand for specific skills of a high order which is often unmet. It has been proposed that a Public-Private Partnership between Government and industry will take up the skills development programme under the name "Skills Development Initiative" or SDI. Details of the scheme will be worked out and announced shortly.

## **IT Hardware**

- The electronics and telecom sectors merit special attention. Of 217 Information Technology Agreement (ITA) bound items, the duty is required to be brought down to nil. Consequently, to provide a level-playing field to the domestic industry, FM proposes to remove the customs duty on specified capital goods and all inputs required for the manufacture of ITA bound items.
- A countervailing duty (CVD) of 4 per cent on all imports is proposed to compensate for the State level taxes, in particular the forthcoming State level VAT, which is proposed to be imposed on corresponding domestic goods. For the present, the proposal is to levy a CVD of 4 per cent only on the imports of ITA bound items and their inputs that attract nil duty. Credit for the CVD will be available against payment of excise duty. However, IT software will be exempt from the proposed CVD.

**SALIENT FEATURES OF THE TRADE ADJUSTMENT ASSISTANCE**

**FOR FIRMS OF THE U.S.**

1. Trade Adjustment Assistance for Firms (TAA), a federal program, provides financial assistance to manufacturers affected by import competition. Sponsored by the U.S. Department of Commerce, this cost sharing federal assistance program pays for half the cost of consultants or industry-specific experts for projects that improve a manufacturer's competitiveness.
2. If an import-impacted manufacturer intends to change its business to better compete, anticipates using consultants to implement these plans and could use a boost in paying for the expertise, then TAA is a good fit. Interested firms begin by contacting one of twelve regional Trade Adjustment Assistance Centers (TAACs).
3. Manufacturers qualify if imports have contributed to declines in employment and sales or production. There are many ways these requirements can be met under the programme.
4. TAA offers 50/50 cost sharing of projects aimed at improving a manufacturer's competitive position. Specifically, these matching funds are applied toward the cost of consultants, engineers, designers or industry experts for improvement projects in areas such as manufacturing, engineering, marketing, information technology and quality. TAA pays for half of the cost of these services, up to \$ 150,000 in projects with a maximum TAA share of \$ 75,000. Actual levels of assistance depend on a variety of factors. Levels of assistance depend on a variety of factors, including size of the firm, nature of proposed projects and availability of program funds. The maximum limit is \$ 150,000 in total project costs, with a TAA share not to exceed \$ 75,000.
5. TAA assists in the following types of projects:
  - i. Manufacturing and engineering
  - ii. Marketing
  - iii. Financial and general management
  - iv. Information Technology.
6. TAA works with a variety of manufacturers and for some, imports represent only a minor challenge. For others, they pose a serious threat. Regardless of the degree of impact, a firm may be eligible if it experienced sales and employment declines at least partially due to imports over the last two years.
7. TAA typically pays 50% of the consulting fees directly to the consultant on behalf of the participating firm.
8. Most often, the participating firm chooses the consultant with concurrence from the TAAC.
9. Most firms receive assistance for more than just one project, depending on the nature and cost of each project. Since they take a customized approach to assisting firms, there are many other industry-specific and company-specific projects that are potentially cost shareable. The TAAC will work with the firm to identify just the right mix of projects to enhance a firm's overall competitiveness, NOT just the import impacted areas of the business.