Competition Distortions in India – A Dossier

(CDI-25: July – September, 2014)

For earlier Dossiers please see: http://cuts-ccier.org/Competition_Distortions_India.htm

Periodic dossiers look at the interface of policy issues which has an impact on competition in India, which can be both negative and positive. News as published is used without verifying their accuracy. The purpose is to flag issues to the layman as well as to the specialised policymakers and regulators, rather than be judgmental about them. This would require greater analysis particularly in terms of cost and benefits.

Dear Readers,

We are pleased to present to you the Competition Distortions Dossier Edition No: 25 for the second quarter: July-September, 2014. As always, we have attempted to capture interesting stories ranging from trade, reforms, development in various economic sectors and industries. The stories reflect a mix-bag of both good and bad practices affecting the economy.

The Prime Minister of India, Narendra Modi in his speech, inaugurating "Make in India" campaign on September 25, 2014 at Vigyan Bhavan, emphasised upon the need to convert India into a manufacturing hub. Concerned with out-flux of businesses from the country, he reiterated that there is a need to instil confidence among businesses at both domestic and international levels.

The attempt of the government, therefore, is to *firstly* make India a manufacturing hub, *secondly* to induce ease of doing business and *thirdly* empower consumers to reap the benefits of competition. In line with this thought, the present dossier analyses various policies and reforms of the government, which either result in producing anticompetitive or pro-competitive outcomes giving a complete picture of the policies of the government. The dossier is divided into categories, within which the issues in question are briefly described and later discussed.

The Prime Minister has time and again, focussed upon the need to put more attention on enhancing solar power generation. Given this, we have discussed the pro-competitive move of the government of not imposing anti-dumping duty on the solar equipments. *Secondly*, we have discussed the need to induce competition by breaking the nearly monopolistic, state-protected entities such as Food Corporation of India and Coal India Limited. Similarly we have also analysed the issue of GST and its impact over consumer and producers alike. *Thirdly*, we have scrutinised issues that fester the various sectors be it dairy, finance, telecommunications or aerospace, attempting to assess issues through the lens of competition. The last section examines the ground reality of the PM's claim to support and create a business environment that is based on mutual trust and support. We have provided examples, such as the pro-competitive Press Note 5 (2014 series), the high-handedness of Haryana government towards MSMEs in Manesar and the much welcome proposal of opening the coal sector to global competition.

The dossier strengthens the need for adoption of a National Competition Policy (NCP) for India, without which the ambition of the government to instil trust in businesses and consumers alike, creating a manufacturing hub and taking development of the country to the next level would remain a distant dream. Further, NCP is important so as to address policy-led competition distortions as covered in the CDD.

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A. Trade Policy

1. India not to Impose Anti-dumping Duty on Solar Panels

The Commerce Ministry duly investigated the matter on imposing anti-dumping duty on solar panels. However, Finance Ministry did not notify the imposition of such duty on imposition of solar panels from four countries. Due to which, India lost the opportunity to impose restrictive duties in order to protect indigenous industry. The recommendation of the Commerce Ministry was opposed by both the Power Minister Piyush Goyal and Road Transport and Highways Minister Nitin Gadkari.

http://www.thehindu.com/business/Economy/india-not-to-impose-antidumping-duty-on-solar-panels-nirmala/article6397475.ece

Food for Thought

Indian government needs to give huge impetus to renewable power generation capacity in order to meet its own ambitions of increasing reliance on renewable energy. Presently, the solar power generation capacity of the equipments that are used in the country is 700-800 MW, which is not enough to keep in pace with government plans. In a protectionist approach, the Ministry of Commerce and Industry intended to impose a restrictive duty on photovoltaic cells imported from US, China, Chinese Taipei and Malaysia. The move of the Minister of not imposing one is a pro trade and competition action.

Proliferation of domestic industries can take place only if they are provided with adequate exposure and technical know-how to manufacture low cost and high efficiency solar panels. This can only be done by way of reverse engineering of the imported photovoltaic cells and other equipment used for power generation. Competition is a two pronged approach. On one hand it facilitates enough players in the market to ensure that the consumer is not devoid of choice and on the other it fosters a culture of innovation that leads to manufacture of better cost-effective products. By imposing higher anti-dumping duty the domestic players would have been left aloof of the advantages of competition and eventually the market would suffer.

Since India, with its ambitious Jawaharlal Nehru National Solar Mission Plan is attempting to become a leader of solar power generation it is imperative that the steps taken by the Power and Finance Ministry towards foreign manufacturers of solar power generation must be nurturing in nature. The positive aspect is that the government has appreciated the advantages of competition and made an attempt to assimilate domestic manufacturers' interest with the requirements of the electricity sector. The government has finally taken the responsibility to build capacity and provide technological know-how to the domestic manufacturers so that they can face and be part of the competition at the same time.

2. Dairy Sector Opposes Free Market Access to New Zealand Products

New Zealand's attempt to secure a preferential trade access into dairy sector of the country has caught attention of the domestic producers. The dairy co-operatives and private sector players are against entry of the players of the country into domestic market through a Free Trade Agreement, especially since that would adversely affect farmers and consumers hard and would also open up Indian dairy market to the volatilities of the international market.

http://www.thehindubusinessline.com/industry-and-economy/agri-biz/dairy-sector-opposes-free-market-access-to-new-zealand-products/article6268523.ece

Food for Thought

Dairy market players in New Zealand are in search of new markets, hence, are making attempts to enter into the Indian market. Indian domestic players in the dairy market, however, have expressed that given India's self-sufficiency, it does not need any imports and argues that the government is taking steps without proper consultation with the domestic players. The Gujarat Co-operative Milk Marketing Federation (GCMMF) has, however, agreed to the transfer of research and development from New Zealand in order to increase their milk production but is against the idea of granting them free access to milk or milk products. The Federation fears that, India could follow in China's footsteps where growth in the indigenous dairy industry dropped significantly after free access was granted to New Zealand.

While the producer interests seem to dominate the discussion the lack of a consumer voice is apparent. Opening the Indian dairy markets and allowing access to New Zealand's dairy products will not only aid in decreasing price however but also increase the choice of products for the consumer.

With regards to producers, increased competition could aid in further improving their competitiveness. In 2013-14, India became a net exporter of dairy products with skimmed milk powder (SMP) shipments of over 120,000 tonnes. However, with the decline in global prices, exports of SMP from India are currently seen as unviable. Increased competition would provide producers with the environment to further improve their production processes to enable them to compete more effectively in the export market. Lastly, while tariff reduction on agricultural imports could be a sensitive issue from the Indian side, this can be overcome by emphasising New Zealand's technological expertise in this sector, and by promoting partnership and technological collaboration between two countries.

B. Sectoral Policy

1. TRAI Okays Sharing of Telecom Spectrum

Sharing of spectrum has been, for long, an unresolved and intriguing issue in the telecom industry. In a present move, the government has allowed the sharing of additional and unused spectrum of the telecom players amongst each other. The issue, however, is that in view of the huge number of customers to cater to; there is hardly any additional spectrum for the players to share.

http://indianexpress.com/article/business/business-others/trai-okays-sharing-of-all-spectrum-categories-by-telecom-companies/

Food for Thought

The Telecom Regulatory Authority of India (TRAI) in a move of late has allowed the sharing of unused spectrum by the companies. The rider in this is that, the companies intending to share must have same type of spectrum. The move by TRAI has been effectuated keeping in mind the interest of the consumers. However, with the move TRAI has also increased the fees payable by the companies to the government by 0.5 percent of their adjusted gross revenues.

On the other hand, companies are not very enthusiastic about the development. They are of the opinion that the telecom industry is very competitive and that the sector players do not have adequate spectrum that can support the proposed sharing. Such paucity in availability of spectrum is visible in the high-price allocated for the procurement of spectrum which already is an issue with the relevant players.

On the contrary, some consider this move as a positive development. They opine that, through the move TRAI has taken cognisance of the challenges that appear when it comes to sharing of spectrum. Challenges such as a coordinated approach to network planning and optimum utilisation of the spectrum would be possible in the present scenario than in the previous conditions when the companies individually procured spectrum. The move is especially interesting because in 2013 itself, TRAI fought a legal battle with Bharti, Vodafone and Idea on the grounds that they had no rights to share spectrum won in the 3G auction. To this, the appellate authority clarified that TRAI cannot dub sharing of spectrum as illegitimate especially in the interest of consumers.

Sharing of spectrum no doubt is positive and pro-competitive approach. Many developed economies around the world adopt this approach to cater to the need of consumers. This approach will foster better spectrum management that would lead to efficient and optimum utilisation of the spectrum by the companies.

2. Modi Government Clears Private Entry into Military Transport Aircraft Project

Defence PSU Hindustan Aeronautics' monopoly in domestic aerospace arena ended with Modi government finally indicating the entry of foreign players (in form of tie-ups with Indian private sector) into the defence aeronautics sector. Presently the collaboration of Indian and foreign entities would be to effectuate supply of 56 transport aircrafts to the Indian Air Force (IAF).

http://timesofindia.indiatimes.com/india/Modi-govt-clears-private-sector-entry-into-military-transport-aircraft-project/articleshow/38686575.cms

Food for Thought

Hindustan Aeronautics Limited (HAL) established in 1940 is the aeronautics and defence company under the management of the Ministry of Defence. HAL enjoys the monopoly in the manufacture and assembly of aircrafts, navigation and communication related equipment. It is well understood, that, aviation is capital intensive and long incubation oriented sector that needs constant innovation. HAL as and when compared to its global counterparts such as Israeli Aircraft Industry or even Embraer of Brazil has not been able to transform into a pioneering aerospace hub. HAL's failures – be it MiG series failure, delay in meeting deadlines, failure to provide state-of-the-art and cutting-edge technology – is legendary. One of the obvious rationales that have led to this dismal state of this Navratna PSU is lack of exposure to competition. Time and again, IAF has pointed out that HAL has not kept itself abreast of time and that the government must introduce a higher cap of FDI into the sector so that better technology and more capital can flow into the aerospace sector.

To make Indian private sector a potential player in aircraft manufacturing sector and to initiate capacity-building of the domestic players, the government has resorted to the present plan. For long Indian companies such as Tata, Reliance, Mahindra and L&T have been eager to enter the aerospace sector and reap the potentials therein. Introduction of more number of players would automatically allow the in-flux of better technology and increase capital in the sector which in turn will foster competition.

In-flux of players into the aerospace sector is no doubt a welcome move. Especially since the government is intending to join up domestic and foreign players. This would not just increase competition, but, would also act as a step to capacitate the domestic players to be abreast of technological changes.

3. Blizzard of Rules by DGCA Threaten to 'Kill' Air Charters

Charter business within the aviation sector is one of the promising commercial activities, that is left at a dismal state. The disheartening state-of-affairs of the charter business is owing to the multitudes of regulations that chain the sector. These rules and regulations make it very cumbersome for establishing and operating businesses.

http://articles.economictimes.indiatimes.com/2014-08-10/news/52648203_1_flying-permit-dgca-aviation-regulator

Food for Thought

Charter business in India, is one of the sector that has a huge potential especially since many companies now want to either enter the commercial aviation sector or else want to expand their current business. However, empathy of the Directorate General of Civil Aviation (DGCA) and the bureaucratic shackles does not allow the business and the entrepreneurs to proliferate.

The cumbersome DGCA regulations result in delay in securing permits that in turn causes delay in starting operations. Also, repetitive and irrelevant checks made during aircraft induction, retard business for the charter aircraft service providers. Operators inducting new type of aircraft have to bear the training costs of inspectors of DCGA to inspect and check functioning of such aircrafts. The abysses of the situation can be interpreted from the fact that operators with one or two aircrafts need to hire as many personnel, similar to the requirement of larger operators.

The existing regulations set by the DGCA do not allow the entry of new entrants. The regulations compel the small operators and businesses to remain under the shadows of the existing large businesses. This allows dominance of the existing businesses in the charter aviation sector. On one hand, the government wants to set up certain significant 'standards' for the charter aviation sector but on the other hand it is decelerating the pace of entry of players by restricting competition in the sector through its high-handedness and improper governance.

Charter aviation, no doubt, needs impetus from the government and the regulator alike, but this is not possible unless spirit of competition is induced into the players as well as the sector itself.

C. Reforms

1. Unshackling the Three Behemoths

The Food Corporation of India (FCI), Coal India Limited (CIL) and Indian Railways monopolise food, fuel and transportation sectors of the country. The monopolistic positions enjoyed by all three institutions allow them to have huge assets and networks under their clutches. It is suggested that, for the betterment of the economy, sector and people at large these entities must be broken into smaller units and privatised.

http://www.livemint.com/Opinion/NJucelZ9pOgHGJQP3OF6iL/Unshackling-the-three-behemoths.html

Food for Thought

Indian Railways, FCI and CIL are the three state owned monopolies or virtual monopolies that have time and again come into limelight either owing to their brobdingnagian structures or because of their vast ambit of power. These companies enjoy vast monopolistic powers that are guaranteed by none other than the government.

The FCI manages around 32.6 million tonnes (rice and wheat as of June 2014), while the FCI coupled with the State agencies together holds 62.2 million tonnes of food grains. Despite this huge stock of food, the FCI is unable to do anything to address the issue of high food inflation. Automatic release of food grain on occasion of rise in prices is not facilitated by the FCI, which should be done logically in the first place. Coupled with this, the procurement patterns of the FCI is also faulty, since it is governed by faulty policies over which it has no control.

Just 2013, the Competition Commission of India had slammed CIL a fine of Rs 1,773 crore for resorting to competition distortionary measures and acting like a monopoly in the coal mining sector. Despite the fact, that, CIL is the largest producer of coal and India possessing 11 times bigger reserves than Indonesia, still the power producers of the country are compelled to import expensive coal to meet their requirements. In absence of proper competition, the giant has no incentive to extract requisite level of the coal.

On a similar footing, the Indian Railways controls track coverage of around 65,000 kms across the country, supporting the largest transit of passengers annually. Like FCI and CIL, Indian Railways too enjoys a monopolistic position which results in the dismal situation of Indian Railways which can be envisaged by the fact that the entity has no profit margin.

The commonality between these three entities is clear, firstly that they are either monopolistic or nearly monopolistic entities with hardly any or no competition and secondly that these entities are owned by a single owner – the Government of India – that does not differentiate between commercial and social goals. The monopolistic tendencies of these three entities are retarding their respective sectors at a considerable rate, wherein the consumer is the final sufferer. Breaking their structure and privatising the respective sectors would instil much required competition. This competition, in turn, would facilitate proliferation, efficiency and efficacy of the sectors as well as that of the economy.

2. States Assured of Making Good GST Losses

Finance Minister, Arun Jaitely has informed the Lok Sabha that the Centre would compensate the state governments on account of losses incurred due to implementation of Goods and Services Tax (GST). Such compensation shall be paid for a period of three years starting from the implementation of the new tax regime. The move of the government is towards ironing out hurdles before effectuation of GST.

http://indianexpress.com/article/business/business-others/govt-assures-states-of-making-good-gst-losses-for-three-years/

Food for Thought

The government is aiming at introducing GST and therefore removing all the impediments on its way. One of the impediments posed by the respective states is that by implementing GST, the states would lose on the revenue. To resolve this issue, the government has proposed the scheme of compensating the states as it had done when Value Added Tax was introduced.

Compensation for Central Sales Tax (CST) is an eye-sore in the Centre-state relations. CST is a tax on inter-state movement of goods that was reduced from four to two percent with the *understanding that the Central Government intends to compensate states for the losses on account of the phase-out. Despite the intent of the Central Government, the states are due to get the compensation since FY 2012 and the budget of FY 2014 allocates an amount of Rs 9,000 crore of which only Rs 1,900 has been released so far.*

The concept of GST is, no doubt, a welcome move from the perspective of consumers. With implementation of GST, consumers would have a wider spectrum of choice of products at reasonable prices. The structure of taxation creates a spirit of competition among the states, which eventually burdens the consumer and consumers' choice. With the implementation of the GST, the burden over consumers of multiple taxes that increase the cost of goods and services will be substantially decreased. However, one must bear in mind that amount compensated to states by the central government for loss of revenue will be out of the government coffers i.e., the compensation will be paid out of the taxpayers' money.

However, looking at the bigger picture, one must appreciate that GST is a pro-consumer and pro-producer move.

D. Industrial Policy

1. Validity of Industrial Licenses Extended

In an attempt to enhance the ease of doing business and simplifying the process of procuring extension to industrial licenses, the government has come up with a new Press Note. This allows the government to extend the period of validity of the industrial licenses from two to three years and has also relaxed the requirement for going back to licensing committees for extensions. Apart from this, additional provision has been made to procure extension with the approval of the Joint Secretary concerned of the administrative ministry.

http://www.thehindu.com/business/Economy/centre-extends-validity-of-industrial-licences/article6170913.ece

Food for Thought

The primary emphasis of the Modi government is on strengthening the manufacturing sector in India. The famous 'Make in India' campaign of the Prime Minister, nonetheless needs more attention. One of the biggest impediment in making India "business–friendly" is to increase the 'ease of doing business' in the country. According to the World Bank ranking on "Ease of Doing Business", India ranks 179 out of 189 – a matter of concern especially if the country aspires to turn into a manufacturing hub. The most significant factor, that, hampers the ease of doing business are the multitude of rules and regulations for starting, maintaining and continuing business in the country. A need is felt across the business community to make doing business as simple as possible.

With the objective of making the process of extending industrial licenses simpler, the Government of India issued Press Note 5 (2014 series). Through the said Press Note, the government has extended the validity of industrial licenses from two to three years and relaxed the requirements for the companies to go to the Licensing Committees for an extension. Also, now the extensions will be provided by the approval of the Joint Secretary of the concerned ministry. The Press Note 5 is applicable to those units too that are valid license-holders but have not yet started production. However, to enjoy the benefits under the Press Note, the industrial units would need to follow certain preconditions.

By taking steps in the direction of change, i.e. from being a consumption based economy to a production based economy, the present government is giving impetus to not just the economy but is also in-turn bolstering competition. By making 'doing business' simpler, *therefore, more and more industrialists would be attracted to the sector. This in turn would enhance competition in the market with the increase in players. The move, therefore, is no doubt a pro-competitive and pro-consumer approach of the government.*

2. Manesar Industrialists Rue Step-Motherly Treatment by Haryana

Members of the Manesar Industrial Welfare Association (MIWA) have raised representation to the Haryana State Industrial and Infrastructure Development Corporation (HSIIDC) in respect to enhancement of land cost from industrialists at the Industrial Model Township (IMT). MIWA has alleged that the increase in the land cost would adversely affect the MSMEs of IMT that are striving to facilitate competition despite the unfair treatment meted out at the hands of the Haryana Government

http://www.thehindu.com/todays-paper/tp-national/tp-newdelhi/manesar-industrialists-rue-stepmotherly-treatment-by-haryana-government/article6161313.ece

Food for Thought

Manesar Industrial Area is a hub that, primarily aims at giving certain additional benefits to Medium, Small and Micro Enterprises (MSMEs). The industrial area supports many such MSMEs. However, the move of the Haryana Government towards increasing the land cost at IMT, Manesar is an issue that deserves to be scrutinised closely. MSMEs in the country are not a very profit-making section of the economy, now with the levy of additional costs it is dubious as to how these MSMEs are going to sustain. It is observed that more than 800 entrepreneurs will be adversely affected by the increase in cost.

Another observation is, that, though the HSIIDC was formed on a 'no profit, no loss' principle. However, the Corporation has made a hefty profit by sale of industrial plots wherein plots worth Rs 12 lakh per acre were sold for Rs 89 lakh per acre. While the government and HSIIDC is charging a huge price to the MSMEs, it gave away the same land to Maruti Suzuki at just Rs 19 lakh per acre.

MSMEs are an integral part of the Indian industry that creates the base for competition in the economy, by catering to consumer needs through cheaper and cost – effective products and services. On one hand, government recognises the need and significance of the MSMEs and also provide incentives for their sustenance and proliferation, but, on the other hand such high-handedness of the Haryana government would impede the pace of the MSMEs. Resultantly, they would shy away from the sector and the consumer will be left at the mercy of the big corporations that indulge in market distortions and adversely affect competition.

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