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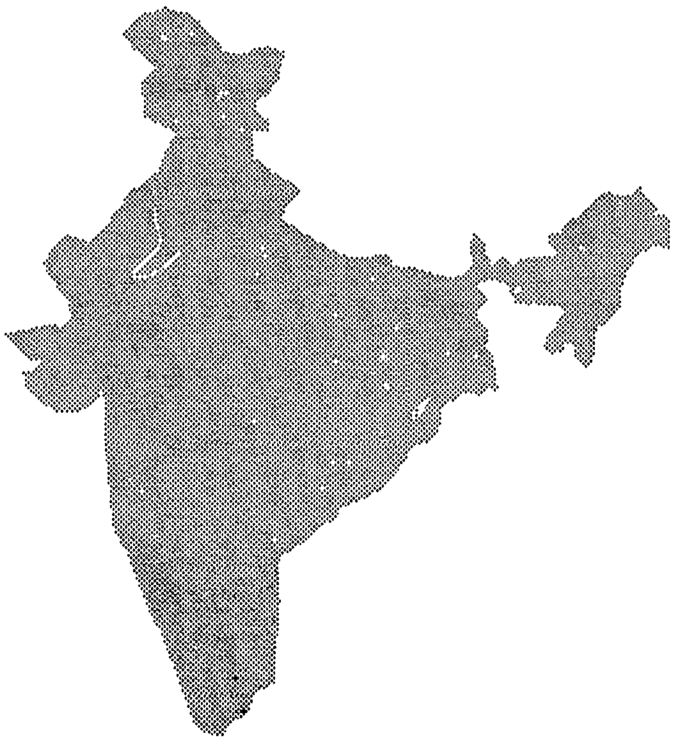

USAID / India

Strategic Framework
FY 1992 - 2000

March 1992

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EXECUTIVE SUMMARY

With vast resources that include a well developed industrial base and a diversified agricultural sector, world renowned manpower and entrepreneurial talent, and a burgeoning middle class numbering 150 million, the Indian economy has long had the main ingredients to achieve rapid broad-based growth. The historic shift now taking place in the Government's policy orientation could provide the key to uncaging India's enormous potential. These changes also hold new hope for the impoverished majority of Indian citizens, who have only marginally benefitted from four decades of centrally-planned state-dominated development.

The bold stabilization measures announced by the minority government of Narasimha Rao in mid-1991 were a direct response to the country's foreign exchange crisis and tumbling international credit ratings. These early measures produced quick results, and proved pivotal in restoring macroeconomic stability and regaining investor confidence. Companion reform measures related to trade, finance and industry mark India's most serious attempt to liberalize its highly regulated economy since independence.

The Government's stabilization and policy reform initiatives have been hailed both in India and abroad. The World Bank, the International Monetary Fund and all other major donors, including the United States, have strongly endorsed these measures. Most observers agree that the reform program constitutes an irreversible new direction in Indian policy, but that disciplined implementation and additional measures will be required to spur economic development and ensure India's closer integration with the global economy.

These policy changes provide an unprecedented opportunity for USAID to assist India in its efforts to become a prosperous, outward-looking country capable of meeting the basic socio-economic needs of its large population. The Mission has identified the acceleration of broad-based, market-led growth as the key goal for the 1990s. Mission activities will focus on three program objectives: an improved financial and regulatory environment, increased productivity of Indian enterprise, and the promotion of smaller, healthier families. These three areas of focus build on the strengths of the existing portfolio. They also reflect new opportunities for high impact interventions created by India's dramatic shift in policy. Figure 1 presents the strategic framework in schematic form.

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Efforts to strengthen India's nascent market-oriented housing finance system will continue as a central intervention under the first program objective. New initiatives to increase the efficiency and promote the expansion of India's capital markets are also a part of these efforts, as are plans to improve the regulatory environment affecting enterprise development. A central element of these latter efforts will be use of Title III local currencies to fund programs that minimize the dislocation of weaker segments of the society resulting from the economic transition now underway.

To help make Indian enterprises more efficient in the newly liberalized and more competitive economy, the Mission will continue to support improved access to productivity-enhancing services and technologies. We will encourage strategic alliances with U.S. firms to help modernize the business operations of Indian enterprises as well. Increased emphasis on energy efficiency and environmentally sound services and technologies will place this program in the forefront of the new Presidential initiative, the U.S. Asian Environmental Partnership.

In working to achieve smaller, healthier families, the Mission will continue programs with both government and private sector organizations that aim to increase contraceptive prevalence and provide improved nutrition and other select health services to high-risk groups. Family planning efforts will concentrate on India's largest state, Uttar Pradesh, in an effort to demonstrate that a village-based, birth spacing approach will contribute to reducing the very high fertility rates in the fast growing Hindi-belt region.

The Mission's proposed strategy for the 1990s draws upon a wide array of financial resources including Development Assistance, PL 480 Titles II and III, and Housing Guarantees. The size of the program is projected to increase moderately to take advantage of the unprecedented opportunities in India at this time. The main constraint to fully realizing the potentials ahead of us is the diminished USDH ceiling, which has dropped sharply in the past five years.

USAID's agenda for the coming decade is infused with a sense of optimism that reflects the increasing likelihood of eradicating the country's deep-rooted problems and abject poverty through social and economic reform. It is based on the recognition that the U.S. has an array of resources that can be especially helpful to India in managing the transition to a competitive market economy and reducing population growth. With the new openness of India, conditions are excellent for a productive and effective economic assistance program during the last decade of this century.

Figure - 1

VISION

INDIA: A TIGER UNCAGED

GOAL

TO ACCELERATE BROAD-BASED MARKET-LED GROWTH

PROGRAM OBJECTIVE

IMPROVED FINANCIAL AND REGULATORY ENVIRONMENT

PROGRAM INTERVENTIONS

* Promote financial market reform and expansion
* Expand private sector participation in housing finance
* Assist implementation of regulatory reforms

PROGRAM OBJECTIVE

INCREASED PRODUCTIVITY OF INDIAN ENTERPRISE

PROGRAM INTERVENTIONS

* Commercialize productivity-enhancing technologies
* Expand modern business management practices
* Reduce energy/environmental constraints to competitiveness

PROGRAM OBJECTIVE

SMALLER, HEALTHIER, FAMILIES

PROGRAM INTERVENTIONS

* Increase contraceptive prevalence
* Expand private health and family planning services
* Decrease the level of malnutrition in high-risk groups

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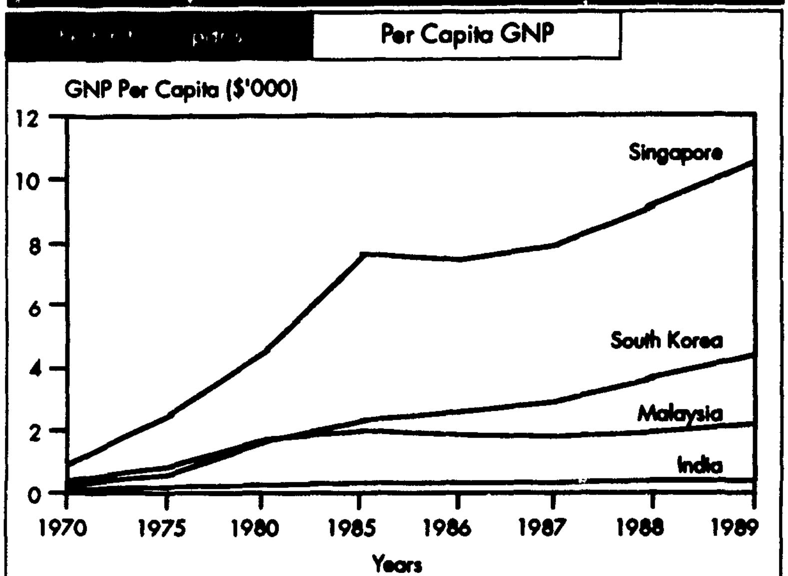
INDIA: A TIGER UNCAGED

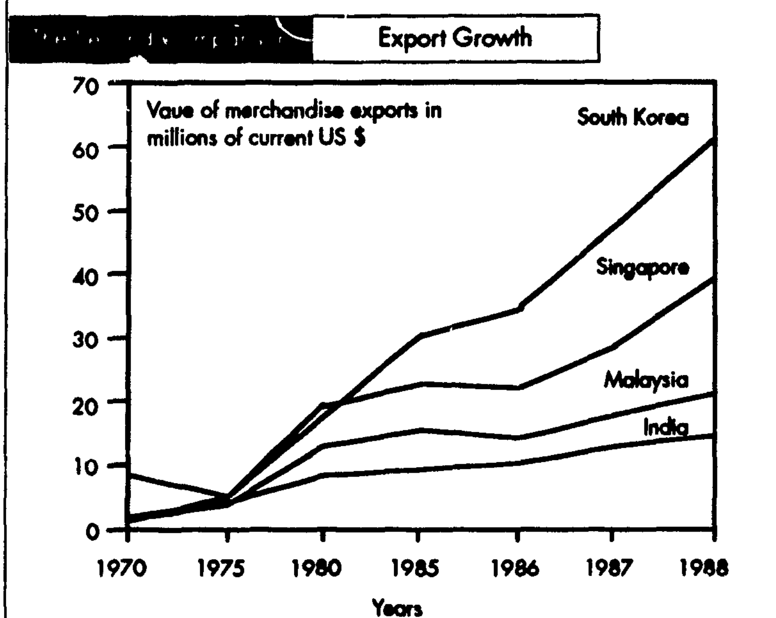
India defies simple description. Unlike most of its counterparts in the developing world, India is a functioning democracy. By one set of accounts, India's development record since independence is impressive. Once the world's largest importer of food grains, India now feeds itself. Owing primarily to annual growth rates during the 1980s of roughly 5 percent, a middle class of some 150 million has emerged. Yet poverty exists on what can only be described as a tragic scale. India is home to one of every four childhood deaths in the world today and two of every five maternal deaths. With its population of 870 million still growing at the rate of over two percent a year, India will eventually overtake China as the world's most populous country. If current fertility trends continue, growth will not stabilize for another 50 years, at which time India's population will have reached 1.9 billion.

The difficult task of portraying modern India has been further confounded by a variety of recent events. Violent conflicts over issues of caste, religion and regional autonomy have occurred on an unprecedented scale. A major economic crisis, with foreign exchange reserves dwindling to less than 14 days of imports, brought India perilously close to defaulting on its international debt obligations. Moreover, the collapse of the socialist model around the world further contributed to uncertainty about the country's economic direction.

In the face of these crises, the mood of the country's leadership grew decidedly self-critical and introspective. Leading news journals depicted India's economy as insulated and crippled by outmoded technology. Only two generations ago, the periodicals noted, India stood economically on par with such "Asian Tigers" as South Korea, Singapore and Malaysia. Yet today, India is far behind these countries in quality of life and economic vitality.

Criticism of India's economic performance culminated in a widely read survey in the May, 1991 Economist. The article concluded that economic policies promoting self-sufficiency and economic isolation were India's undoing, and criticized the omnipresent bureaucracy for stifling private enterprise and throttling individual initiative. Other analysts followed suit,





Source : World Tables 1991

arguing that the government had to quickly and irrevocably abandon its state-led, capital-intensive "command and control" approach to economic development and instead adopt a more outward-looking, private-sector-led strategy.

With the support of the main opposition party, the minority government of Narasimha Rao (which came to power in June, 1991) acted swiftly on these recommendations. In his State of the Union address to Parliament, Rao announced a radical agenda for reform, declaring that his government "will work to make India internationally competitive." He extended an invitation to foreign investors, outlining his vision of a "vibrant economy that rewards creativity, enterprise and innovativeness." Important reform measures followed, and more are in the offing.

Rao's bold new policy measures have been hailed both in India and abroad. The consensus of the IMF and the World Bank, as well as all major bilateral donors, is that these reforms represent a historic and irreversible new direction in Indian policy. But the enthusiasm is tempered with recognition that the transition process will be painful. It will take disciplined implementation of the reform policies over the next several years before India's economy becomes as healthy and vigorous as its Asian neighbors. It will also require a major reorientation in the feudal-like attitudes many Indians have towards government and their local leaders.

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The strategy proposed in this document reflects the historic development opportunities that now exist, and the vital role USAID can play in helping India to become a modern, prosperous and outward-looking country, more closely integrated with the world economy – in short a tiger uncaged.

Over the next five years, the country should make major inroads against the chronic poverty that affects the majority of its people. Many Indians can hope to benefit from rapidly expanding employment and income opportunities resulting from the policy reforms. Improvements in social services, including much greater participation of the private sector, should enable many more households to meet their basic health, family planning and educational needs. Accelerated, broad-based development should also lead to closer integration with the global economy and provide strong incentives for increased commercial ties with the U.S. based on expanding trade and rising foreign investment levels.

II

ACCELERATE BROAD-BASED MARKET-LED GROWTH

"India is not poor by nature, but poor by policy." This observation, made by a former Indian Ambassador to the United States, speaks of an economic paradox — despite the country's rich natural resources, its well developed agricultural and industrial sectors, and its world renowned manpower and entrepreneurial talent, India's economic performance over the past four decades has fallen far short of its tremendous potential.

Approximately 55 percent of the population, over 425 million Indians, are poor, and 33 percent, or approximately 280 million, are extremely poor. To be poor in India can mean many things. For women in remote Rajasthan, it means one chance in ten of being literate; for a young child in a poor family, the world's worst odds for living beyond the age of five; for most workers with two to three dependents, an income of less than $30 per month. It is these people, whose status has remained largely untouched since independence, who stand to benefit most from the economic changes now taking place in India.

For the past 40 years, central planning boards have effectively usurped the role of market forces in the Indian economy. The country's economic policies have restricted trade, protected local manufacturers from foreign competition and reserved the "commanding heights" of the economy for state-owned enterprises.

For India to realize its vast economic potential — to optimize its natural resources, its large-scale capital investments, and reduce poverty — it must first dismantle the "cage" of existing economic controls. The recent liberalization measures announced by the Rao government, coupled with the new macro-economic stabilization efforts, are important first steps. These reforms have:

- Made it easier for new firms to enter a sector and existing firms to expand their operations by abolishing most industrial licensing and reducing restrictive practices that limit the growth of existing businesses;

- Encouraged foreign investment in high priority industries by allowing up to 51 percent foreign equity ownership, automatic approval of technology agreements in certain industries and much larger royalty payments; and

- Freed foreign trade from government interference and initiated steps to make the rupee fully convertible.

THE TIGER CAN RUN!

In the mid-1980s, the Rajiv Gandhi government proved that the Indian economy can perform better. Even though Gandhi's economic reforms were minimal, he doubled the GNP growth rate and per capita income, increased exports faster than ever before, dramatically expanded capital markets, and improved the overall levels of literacy, infant mortality, and poverty. When such significant benefits result from such small changes, it is obvious that the Indian tiger can run – if allowed to.

These policies mark a fundamental break with the past. The reforms have been accompanied by a new openness to private sector participation in the full gamut of development efforts, including basic health care and family planning. The measures also reflect a renewed willingness to reassess the efficiency and effectiveness of social development programs to improve their impact.

These efforts, however, represent only a beginning in the transformation of India's development equation. Additional reforms will be essential to ensure a rapid transition toward a market-oriented, outward-looking and rapidly growing economy. Such areas as tariff structures and trade regulations are still in need of greater liberalization. Initial measures to strengthen the financial sector must be followed up by further deregulation of banking activities and expanded private sector participation. And, if industrial reforms are to achieve their maximum impact, firms must not only be assured "freedom of entry" into the market, but "freedom of exit" as well.

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USAID has long advocated the kind of changes the Rao government has recently initiated. We believe that such measures are essential to establish the foundations for sustainable development in India. Accordingly, the overarching goal for our program in the 1990s is to accelerate broad-based market-led growth. To achieve this goal, the Mission will focus on three primary objectives :

1. **Improving the financial and regulatory environment**
2. **Increasing the productivity of Indian firms**
3. **Promoting smaller, healthier Indian families**

While these objectives have firm roots in the Mission's existing portfolio, today they reflect the important new opportunities for high-impact interventions created by India's dramatic shift in policy. USAID goals demonstrate strong support for the reform movement and are aimed at minimizing the near-term costs of change for firms adapting to an open and competitive business environment and for minimizing the dislocation of employees. Mission efforts are also focused on ensuring the sustainability of India's new economic course via efforts to reduce family size, encourage environmentally sound production technologies, and secure mutually beneficial partnerships with organizations in the U.S. that stimulate ongoing innovation and problem-solving.

The first program objective of an improved financial and regulatory environment addresses two related areas in need of immediate reform: financial markets and industrial regulation. Despite India's considerable success in mobilizing personal savings, its financial system has been seriously weakened by policies which have funnelled valuable investment resources into inefficient enterprises. USAID's decision to focus on these areas reflects both the close associations the Mission has developed with India's leading financial institutions over the past five years, and the government's acknowledgement of the need for reform in these areas.

Efforts to enhance the productivity of Indian enterprises, the second program objective, represent a continuation of the Mission's highly innovative activities in the areas of technology and energy. India's new market orientation and critical need to promote exports place these efforts at the center of change. The success and political viability of liberalization will depend in great part on the increased efficiency and productivity of local firms. Accordingly, the Mission plans to expand its focus on technology development to include a business service orientation that will help firms adapt more quickly to a market-driven economy. By lending an environmentally focused eye to these activities, the Mission will be in the forefront of the President's new Asian Environmental Partnership, described in Section VI.

The Mission's final program objective, to promote smaller, healthier families, addresses two of India's most intractable problems – rapid population growth and high infant mortality – both of which have a corrosive effect on the country's long-term development prospects. The willingness of the government to rethink past approaches to these problems and AID's impressive record of accomplishments in these areas are critical factors in the decision to allocate significant Development Assistance (DA) resources to these activities. An additional component of this program is our continued partnership with CARE and Catholic Relief Services to reduce the level of malnutrition in high-risk groups.

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III

PROGRAM OBJECTIVE NO. 1:

IMPROVED FINANCIAL AND REGULATORY ENVIRONMENT

India's macro-economic crisis of 1991, caused by unsustainable fiscal and current account deficits and aggravated by events in the Persian Gulf, has left little doubt regarding the course the country's economic development must take. Policy-makers no longer have "soft options" at their disposal and must introduce strong measures to adjust the economy. The primary purpose of the Mission's first program objective is to support these changes by concentrating on financial sector reforms and on improvements in the regulatory environment affecting enterprise operations. It should be emphasized that Mission efforts can only be described as modest in light of the enormous challenge India faces in these areas. Still, we believe our assistance will provide important contributions to institutions and organizations that advocate reform and have much at stake in India's rapidly changing economic environment.

Dating back to Jawaharlal Nehru's introduction of economic self-reliance in the early years of independence, Indian policy-makers have developed a vast and intrusive system of regulatory and financial controls. The system banned most imports to protect local industry from international competition and channeled investment into the production of capital goods and equipment by public sector companies unconcerned with the dictates of supply and demand. Private sector industrialists were required to follow a regime of licenses and controls that influenced such basic enterprise decisions as what and where to produce, and how much to charge for output.

The perverse consequences of these policies are aptly illustrated in the experience of one Indian industrialist who explained that although his plant could optimally employ 1600 workers, he was afraid to hire such a large number of employees because of his inability to retrench during periods of economic slowdown. Instead, he invested his capital in machinery and limited the number of employees to 400. These 400 workers have jobs with life-long security, but there are another 1200 would-be employees who, as a result of the Government's interference in this firm's operations, do not have any jobs at all.

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The tight regulatory environment confronting Indian businessmen was in many ways sustained by equally intrusive financial sector policies. Following the nationalization of the banking system in the late 1960s, lending institutions were obliged to provide subsidized credit to priority sectors and inefficient public sector clients. As a result, many banks hold loan portfolios that are riddled with bad debts to "sick" companies that require capital infusions to maintain their inefficient and unprofitable operations and are unable to close down because of government regulations.

As a result of these actions, the financial sector is in danger of becoming insolvent. The one exception, however, is capital markets area, which has witnessed unprecedented growth in the last decade. Market capitalization rose to $40 billion in 1990, up from $16 billion only three years earlier. The capital markets are a critical source of investment to finance India's future economic expansion.

THE "SICK" INDUSTRY SYNDROME

At the end of 1987 there were 160,000 "Sick Units" firms that were currently making losses and whose liabilities exceeded their assets. The choices for such firms were limited. Takeovers and mergers ... are tightly controlled to ensure that they are in the "public interest" ... Asset sales are difficult, land sales often impossible. Permission is needed to sack workers, and is granted sparingly. "Financial difficulty" is explicitly ruled out as a basis for application to dismiss workers. Many owners simply walk away, taking with them any movable assets, leaving the rest to decay and the employees to fend for themselves. But most sick firms are kept alive with subsidies, tax reliefs and credit extended by the state-owned banks.

Excerpt from the May 4 Edition of The Economist.

PROGRAM STRATEGY

Substantial improvements in the financial and regulatory environment will be required to serve the increasingly complex needs of Indian industry, agriculture, housing and trade. Financial institutions will require more autonomy in their operations and a shift in orientation from social to commercial banking. Incentives are needed to encourage expanded private sector participation in the financial sector. Significant improvements in the operations of India's capital markets are also required, with top priority given to increased transparency and improved efficiency of transactions. Many of these changes are included in the recommendations of the Government's recently commissioned study of the financial sector.

The Government has already announced a series of reforms aimed at improving the regulatory environment affecting enterprise development. These reforms should increase competition by providing greater ease of entry for both domestic and foreign producers and simplifying access to new productivity enhancing technologies. The result will be greater pressure on inefficient and unprofitable operations now propped up by public sector lending institutions. An exit policy that allows these "sick" firms to shut their doors or sharply scale back operations, including retrenching surplus labor, will be essential if the new industrial policy reform package is to succeed.

❑ Financial Market Reform and Expansion

USAID has a long association with India's leading financial institutions and has made important contributions to the development of its financial markets. India's new venture capital industry, whose importance looms larger in light of the more competitive environment domestic industries now face, is a direct outgrowth of Mission efforts to promote investment in commercialization of new technologies.

The Mission is preparing activities supportive of India's burgeoning capital markets, including technical consultancy and training programs. India's capital markets raised over $5 billion in 1991, up from $100 million a decade earlier, and liberalization measures point to an even brighter future for this industry. To realize the potential of India's capital markets, improved operations and regulations are required. USAID will assist in this process by concentrating on:

(1) Establishing a national depository system to increase the operational efficiency of India's 23 stock exchanges; and
(2) Increasing access of small and medium firms to capital markets through the creation of an "Over The Counter" market.

THE BULL RUN

So far, for the Indian stock market, this is the best year yet. With the bulls on the Indian bourse hitting the ring, members of the brokering community have reaped rich harvests, as have the ten million investors. Notwithstanding this euphoria, only about one percent of the country's savings flow to the capital markets – a marginal amount for a country with one of the world's highest savings rates (21 percent of the GDP). The Indian investor is just beginning to understand that bullion and real estate do not match the exponential growth in stock market returns. Expectations are high, and in all likelihood more money will flow through the capital market to fuel a further surge. Many feel the best is yet to come.

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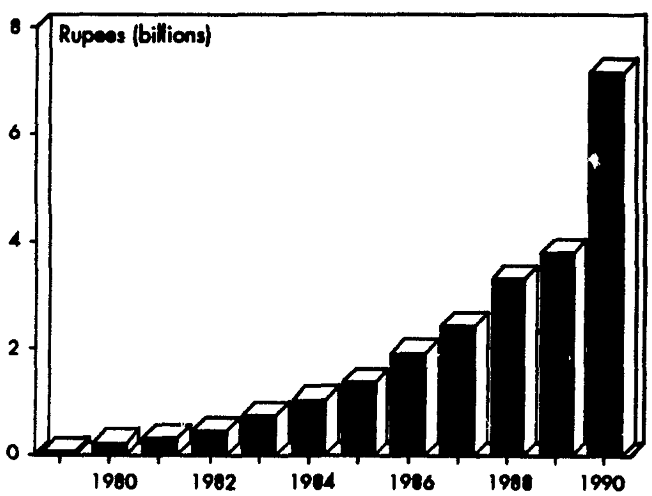
The Mission expects the Government to introduce major financial sector reforms in the coming six months. In order to create a modern banking system, these reforms must be accompanied by a new system of prudential regulations to encourage competition and promote a commercial orientation. The Mission is examining ways to assist with the introduction of these new prudential regulati.

❑ **Expanded Private Sector Participation in Housing Finance.**

HOUSING FINANCE SYSTEM EXPANDS RAPIDLY

The private sector housing finance system in India has expanded rapidly since USAID's assistance to the sector began in 1981. From only one registered housing finance company in 1979 with a loan volume of $2 million, the system has grown to include more than 250 companies and 136 branch offices with over $300 million in loans in 1990. USAID's housing guarantees, expert advice, and training have had a significant impact on developing the rules by which the system operates and have increased the availability of housing finance. Moreover, our programs have demonstrated the viability of lending to below median income households: more than 50 percent of all private housing finance company loans have gone to these households, and one quarter of all borrowers are low income families.

Total Loan Volume Sanctioned By Market-Oriented HFCs



USAID has significantly contributed to the rapid expansion of the national housing finance system. This system has provided a highly visible example of successful market-rate lending and was often cited in government discussions that resulted in the deregulation of interest rates for the entire financial sector.

Housing finance will remain a central component of Mission efforts to improve the financial and regulatory environment. Specific aims of the future program include increased financial resources mobilized by the housing sector, expansion of market-oriented housing finance institutions, and an expanded supply of housing finance to low-income households.

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❑ Regulatory Reform

One of the most important features of India's financial and industrial sector reform programs will be the establishment of an "exit policy" to allow inefficient public and private sector enterprises to go out of business. Because of the political sensitivity of this subject, the government has moved cautiously in developing its plans for reform. The most vociferous opponents of an exit policy are trade union leaders whose supporters have an obvious stake in maintaining the job security virtually guaranteed under the current system. In order to assist retrenched workers, as well as minimize opposition to the exit policy, the government has announced plans to establish a National Renewal Fund to provide a safety net for displaced workers. A central element of Mission efforts is a new PL 480 Title III program, which will facilitate implementation of an "exit policy" by generating local currency to help finance National Renewal Fund activities. Transfer of the Title III local currencies to the National Renewal Fund will depend on achievement of specific benchmarks that are linked to implementation of an "exit policy."

Another component of our support for deregulation is assistance to private sector organizations and associations that have much to gain from opening up the economy. Because these groups have adapted to the "command and control" economic system of the past, they have limited experience with the complexities of an open and competitive business environment. The Mission plans to support new linkages between Indian private sector organizations and their U.S. counterparts to strengthen their understanding of issues regarding competitiveness and productivity and enable them to influence policy deliberations.

The Mission also plans to provide assistance to Indian academic and policy research institutions to ensure well informed public debate and policy determinations associated with the reform package. Again, linkages with U.S. institutions with similar research interests will be encouraged.

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PROGRAM INDICATORS

1. Total Loan Volume Sanctioned by Market-Oriented Housing Finance Companies (HFCs)

Total loan volume is the primary indicator of growth in the housing finance system. By further narrowing this indicator to the loan volume sanctioned by market-oriented HFCs, the data can capture both the growth of the system as well as the shift towards a more commercial orientation by its leading institutions.

2. Total Capital Market Investment in Small and Medium Companies

Capital markets will become an increasingly important source of investment in India's deregulated economy. USAID efforts to increase competition and improve operations and regulations will help ensure optimum resource allocation under this system. Increased investment in small and medium companies with active issues on India's stock exchanges captures both the growth as well as improved efficiency which we are promoting in our capital market activities.

3. An Improved Policy and Regulatory Environment

Many indicators exist to track the overall progress of India's reforms. It would be inappropriate, however, to directly attribute changes in these indicators to USAID programs. To monitor our progress in promoting policy and regulatory reforms, we will provide a narrative recap of our association with key reform events as part of each year's Program Performance Information System (PPIS) submission.

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IV

PROGRAM OBJECTIVE NO. 2:

INCREASED PRODUCTIVITY OF INDIAN ENTERPRISES

A basic aim of India's economic reforms is to end the isolation, technological stagnation and gross inefficiencies of Indian enterprise. USAID has focussed on these same objectives since the mid-1980s, when technology and enterprise development emerged as a central component of our portfolio. A liberalized Indian economy opens up new vistas for USAID efforts to encourage innovation, efficiency and productivity in Indian enterprises. Building on highly successful programs already in place, USAID will continue to support activities aimed at increasing the productivity of Indian enterprises.

Currently, India lags far behind its progressive Asian neighbors across virtually the entire spectrum of industrial activity. The vast majority of locally manufactured goods are made under license from foreign designs. Indian firms fall far below international "best practice" standards in terms of technology, scale, and efficiency, and offer products at high prices and variable quality. With a sophisticated scientific and engineering establishment and a large, diversified industrial base, India has the potential to become a major source of innovation and competitiveness. The problems within Indian industry go far beyond technological stagnation; years of bureaucratic controls, nationalized banks and protected markets have weakened the very fabric of business management skills and know-how in the private sector. Modern marketing skills, relationships with

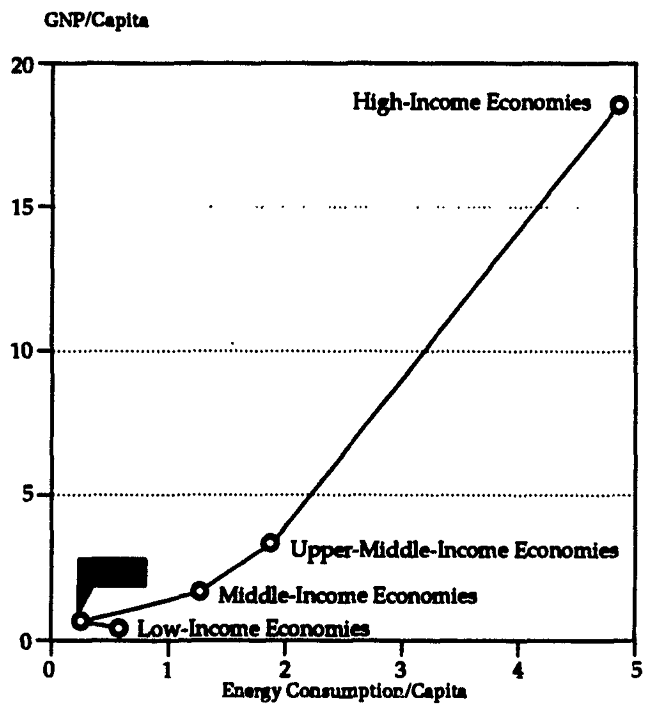
INDIA'S TECHNOLOGICAL INERTIA

The adverse effects of India's technological and competitive inertia are everywhere in evidence. Agribusiness typifies the problem. Only two percent of the 75 million tons of fruits and vegetables grown annually in India are processed due to the lack of handling and storage facilities, and inadequate washing, sorting, grading, and packing technologies. Everyone loses: consumers pay more for inferior produce; returns to farmers for high-value crops are much less than they could be, and India, despite being the world's second largest vegetable producer and third largest fruit producer, garners a mere 0.4 percent share of the $23 billion world market. While enterprises currently remain in operation despite mediocre products and inefficient practices, in an open and competitive environment, they will require rapid movement towards modern, efficient and profitable operations.

suppliers, creative financial engineering, increased participation by labor in the running of enterprises, and achieving just-in-time inventory control are just a few examples of the business skills which require upgrading for Indian enterprises to compete in the global marketplace.

A liberalized Indian trade regime and increased direct foreign investment will force local enterprises to rethink their business strategies. Alliances with foreign enterprises are likely to become a key means of increasing the competitiveness of outward-looking, export-oriented firms. Such relationships will provide direct access to new markets and modern management practices and enable Indian firms to earn the foreign exchange needed to modernize operations. The U.S. is currently India's largest trading partner and foreign investor, and is likely to remain the key source for local enterprises eager to improve their competitive position.

Energy availability will be a critical ingredient in India's drive for accelerated economic growth. Programs to increase India's energy supply as well as improve efficiency and conservation are key components of the Mission's overall program to increase the efficiency of Indian enterprises.



Source : World Development Report 91

Two constraints on Indian businesses are energy shortages and environmental degradation. The Federation of Indian Chambers of Commerce and Industry estimates that annual production losses due to energy shortages amount to approximately 1.5 percent of GDP. To overcome these shortages and respond to growing energy demands in the coming decade, the government estimates that $150 billion of new investments in power generation are required, which is equivalent to 30 percent of total public outlays during the 1990s. In this era of fiscal restraint, such sums are clearly out of the question, and India must find alternate solutions to its energy problems. Options include placing much greater emphasis on energy efficiency and end-use conservation, but these will require the replacement of obsolete process and product technologies. Fortunately, policy makers recognize the need to update equipment, and efforts are underway to encourage foreign investment in India's power sector and to stimulate the commercialization of energy efficient technologies including cogeneration. The U.S. has a major role to play in these efforts.

The ability of Indian firms to be competitive in both the near term and the long term is closely linked to the country's rapidly deteriorating environmental situation. Low productivity and poor quality products are often directly associated with environmentally unsound practices. Indian leather products, for example, have recently been rejected by the European Economic Community countries because the hides contain phenochlorohol (PCP) chemical residues from the tanning process. In other instances, major industrial sites are threatened by large scale hazardous waste contamination. In certain industrial areas, firms must treat and recycle the water they use in order to meet their processing requirements because the water pumped from the ground is so contaminated that it exceeds both production process parameters and permissible standards for effluent discharge after processing.

In response to India's worsening environmental situation, particularly industrial pollution, the Government has issued a series of new policies and regulations to strengthen environmental standards for industrial operations. Numerous firms, ranging from large chemical manufacturers to small agro-processors, are being threatened with closure due to flagrant violations of environmental standards. For many of these firms, compliance with these new standards is greatly hampered by the limited availability of technologies in the local market.

The solution to this problem lies in the liberalization of policies affecting technology transfer. At the same time, efforts are required to inform local entrepreneurs of the range of productivity-enhancing and environmentally safe technologies and services that exist in countries such as the United States.

POLLUTION PREVENTION PAYS

Cost-effective remedies to pollution are available in the United States and other developed countries, and can be transferred to India without jeopardizing the competitiveness of local enterprise. Many components of the new generation of clean technologies, such as "waste minimization," are financially attractive. One example of a technology appropriate for India is a U.S. chemical recovery system for small paper mills. With an investment of $600,000 in this process, the mill can recover over $1.2 million in recyclable chemicals, significantly increasing its efficiency and enabling the plant owner to comply with rigorous environmental regulation of industrial pollutants. In India, few manufacturers are aware that technology exists to prevent the widespread environmental degradation common in paper production areas.

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PROGRAM STRATEGY

The success of India's policy reforms rests, to a great extent, with Indian enterprise. Many changes must occur before local industry can become the lead engine in India's drive for accelerated market-led growth. Protectionist policies of the past have created enterprises that are slow to respond to change and are unfamiliar with the ways of international business. If Indian enterprises are to become dynamic and competitive, they will require access to state-of-the-art technologies and modern business techniques to bring their products up to global standards, including those of environmental soundness. The chief aim of the Mission's second program objective is to support the increased productivity of Indian enterprises as the primary vehicle for achieving accelerated broad-based market-led growth. This will be accompanied by promotion of Indo-U.S. business partnerships linked to competitive business practices in key areas of Mission concern.

❑ Productivity-Enhancing Technologies

India's impressive accomplishments in basic research and high technology areas are well documented. Unfortunately, performance in commercializing new productivity-enhancing technologies has been far less successful. Once installed, machines and equipment are rarely rendered redundant through the introduction of superior technologies. The steel industry demonstrates the consequences of this technological inertia. India installed three "best practice" steel plants in the late 1960s. A decade later they were due for renovation but nothing was done. Soon after, countries like South Korea were selling steel on the world markets at half the production cost of Indian steel. This situation still persists today.

JOINING FORCES TO COMMERCIALIZE NEW TECHNOLOGIES

The USAID-supported joint undertaking between Globe Auto Ltd., Bombay and Scott Motors Inc., Alamogordo is an excellent example of how two small companies can combine forces to develop a new product. This joint venture has resulted in the development of a permanent magnet alternator, with development costs considerably lower than would be possible in the U.S. Permanent magnet alternators with a capacity up to 150 amps. are now available in India, and have important automotive, railway, and refrigeration applications. Globe and Scott have patented the alternator design in India and the U.S., and they also plan to license the production of these alternators in the U.K. and other European countries.

The Mission is currently engaged in several highly successful efforts to strengthen India's capabilities to develop and commercialize new products and processes. In its earlier phase, the main objective of these efforts was to shift the emphasis of India's substantial R&D investments from basic research to product and process development and quality improvement. To achieve this, the strategy encouraged a transfer of decision-making regarding technology development from the Government to the enterprises themselves.

While much remains to be done, the Mission has established an impressive record of accomplishments in stimulating technology development. One example is the growth of the fledgling venture capital industry, referred to on page 10, which makes finance available for firms eager to test new technologies in the marketplace. Other examples include over 30 Indo-U.S. joint ventures to commercialize products and processes resulting from a new market orientation of R&D investments. These efforts will continue to play a central role in the Mission's future program and will be coupled with a new emphasis on strategic technology acquisition to promote commercialization of productivity-enhancing technologies.

❑ Modern Business Management Practices

The open and competitive system that the new economic policy reforms will create will pose significant challenges for Indian entrepreneurs unaccustomed to the demands of a market economy. In addition to the adoption of new cost-effective technologies, enterprises eager to enhance their competitive position will also require access to an array of modern business services that are not readily available in India, such as marketing, creative financial engineering, and just-in-time inventory control.

A second component of Mission efforts to enhance competitiveness will be to stimulate commercial ties with U.S. firms that can assist with modernizing of their operations. USAID activities supportive of agribusiness development and energy efficiency and conservation already include funding to develop these linkages. New initiatives in this area will be considered in the coming year.

RESTRUCTURING INDIAN ENTERPRISES

To date, over 100 International Executive Service Corps volunteer executives have provided assistance to private sector Indian companies to improve operations and increase productivity. IESC's impact has been substantial; in one instance, manufacturing costs have been reduced by 15 percent, and the firm estimates a resultant $5 million annual increase in sales. In another case, an enterprise reports cost-savings of 28 percent, and will establish an in-house R&D department to continue modification of its operations. A new component of the IESC program will be to use volunteer executives to help Indian enterprises identify potential U.S. partners for joint ventures and to recommend U.S. machinery and equipment to enhance the competitiveness of local firms.

USAID

INDIA

❑ Energy and Environmental Constraints

Both energy shortages and environmental degradation directly affect the competitiveness of Indian enterprises, and put basic production systems in danger of collapse from strained resources. The two concerns are inextricably related: energy production is a major cause of pollution, while environmental concerns are a major constraint to development of new energy resources.

USAID's current strategy to address these problems emphasizes energy efficiency improvements associated with supply, distribution and end-use; support for private sector participation in energy development through policy and institutional change; and promotion of sound environmental practices in energy planning and development. Given the recent policy changes which encourage foreign investment in the energy sector, we will look for opportunities to facilitate U.S. investment in this area. A new program currently under design will assist Indian firms in reducing environmental constraints to productivity through acquisition of environmental services and technologies based on commercial agreements between Indian and U.S. firms.

PROGRAM INDICATORS

1. Increased Expenditures on Private Sector Industrial R&D

The level of private sector R&D investment — a significant determinant of efficiency and competitiveness of Indian enterprises — has been low, due primarily to extensive industrial licensing regulations that discouraged private initiative and resulted in technological and competitive inertia. Increased private sector industrial R&D expenditures will reflect that commercial R&D is profitable and that Indian entrepreneurs are responding to opportunities created by recent industrial policy reforms.

2. Increased Private Investment in Environmental Technologies and Power

As a part of its policy reforms, the GOI now permits up to 100 percent private investment (including foreign investment) in India's power sector, which was earlier the exclusive preserve of the public sector. This program indicator will capture two distinct influences: access to environmentally sound technologies, and an increased role of the private sector in the power sector.

3. Increased U.S. Share in India's Foreign Trade and Investment

The U.S. is India's largest trading partner and investor, and is an important source of new technologies. Increased Indo-U.S. trade and investment cooperation — measured by this program indicator — will reflect generally the implementation of recent policy reforms, and specifically the U.S. contribution to promoting Indian joint ventures in R&D. While computing the composite U.S. share, we propose to give equal weight to trade and investment.

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PROGRAM OBJECTIVE NO. 3:
SMALLER, HEALTHIER FAMILIES

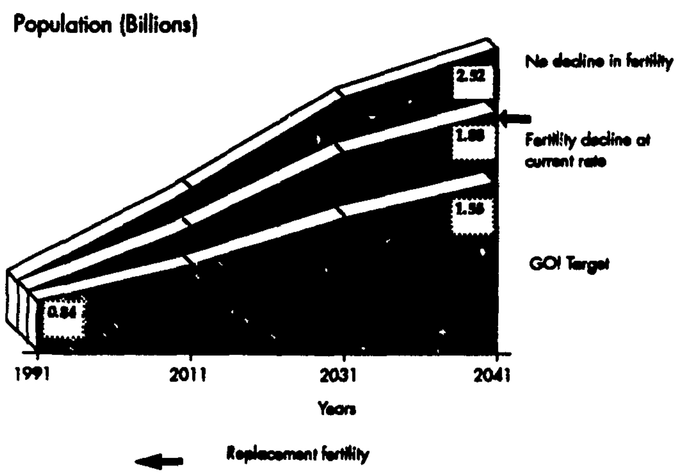
India was the first country in the world to establish a national family planning program. Like the country's economy, however, the program has remained in something of a time warp for the past two decades. If liberalization measures are to succeed in improving living standards of the majority of Indians, similarly dramatic changes must be made to check the rate of population growth. USAID has long been involved in programs that promote smaller, healthier families, and the Mission plans to step up efforts to establish a state-of-the-art family planning program in targeted areas, while continuing other public health efforts related to this objective.

Results of the 1991 census indicate that India's population problem may be even more acute than previously thought. There are presently over 25 million births per year in India, and in the last decade, 178 million people were added to the population — more than in the three decades between 1931 and 1961. With a growth rate of over 2.1 percent per year, India's population of 870 million will surpass the billion mark by the end of the century. The two fastest growing segments of Indian society are the under-15 age group and the over-60 age group. Together they account for 42 percent of the population and represent a huge double dependency for the country's wage earners. Meanwhile, female illiteracy remains very high, especially in the Hindi-belt states. Based on these trends, there is a distinct possibility that

POPULATION PROFILE

Demographically, India is two countries. While over half the country is well into the demographic transition from high fertility/mortality to low fertility/mortality, the other half has barely entered it. The latter group is represented by the four contiguous Hindi-belt states of the north – Bihar, Uttar Pradesh, Rajasthan and Madhya Pradesh – which alone account for 40 percent of India's population. The continuing high fertility and high but slowly declining mortality of these states effectively off-sets fertility decline in the rest of the country. If current trends continue, it will be at least 50 years before these states move through the demographic transition and the country's population is stabilized.

Projected Population Growth (1991-2041)



Source : Rapid III Project Projections

on these trends, there is a distinct possibility that India's population growth rate will actually begin to increase in the 1990s.

The socio-economic implications of an increase in India's population growth rate are truly staggering. Rapid population growth has already complicated the country's ability to deal more effectively with lowering infant and child mortality. Mortality under the age of five in India is over ten times that of any other age group up to the age of 60 and accounts for half of all deaths in the country. Malnutrition and infectious and parasitic diseases kill a large percentage of these children. High birth rates outstrip the ability of public health organizations to deliver immunizations and other potentially lifesaving measures. The high number of women having too many children and receiving poor prenatal care also substantially contributes to the problem. Conversely, high infant mortality impedes ready acceptance of family planning practices by eligible couples, further eroding efforts to stem population growth.

A startling new factor that may impact India's development prospects is the spread of AIDS. Current estimates put the number of people infected with the HIV virus in India at 300,000 to one million. Many experts predict that the virus' course in India will be similar to that in many African countries. If this happens, not only will the public health gains of the last 40 years be jeopardized, but India's development efforts could be further constrained by the loss of a large number of economically productive members of society.

PROGRAM STRATEGY

Notwithstanding the creation of a more open and competitive economic framework, rapid population growth will thwart India's economic expansion and inhibit the ability of a broad spectrum of Indian society to participate in and enjoy the fruits of market-led growth. Achievement of the Mission's goal to accelerate broad-based market-led growth requires increased concentration on efforts to promote smaller, healthier families. As a means to this end, the Mission will aim to increase contraceptive use, increase the number of families receiving assistance from non-government sources, and decrease the incidence of malnutrition. The continued emphasis on healthier families reflects the synergistic relationship between family size and family health.

PRIVATE HEALTH PRACTITIONERS TAKE THE LEAD!

The Indian Medical Association (IMA), with a membership of over 85,000 ph' sicians nationwide, is about to demonstrate the power of the private sector to provide vitally important family planning services. With USAID assistance, the IMA has begun to train its membership to deliver modern methods of birth spacing, emphasising oral contraceptives. IMA's target is to have 50,000 members providing family planning services in the next few years to as many as 45 million married couples of reproductive age. After demonstrating the important role that private practitioners of western medicine can play in India's family planning program, IMA's attention will be turned to mobilizing India's traditional medical practitioners who number over one million. Combined, these practitioners serve many more people than government services can ever hope to reach, and can no longer be overlooked if India is to solve its population problem.

- Birth spacing techniques to enroll young couples in the program and clearly link family planning with family well-being, particularly child survival.

- An expanded role for and participation of the private sector in delivering family planning services.

❑ Expanded Private Health and Family Planning Services

The government is also showing a much greater willingness to accept mounting evidence of an AIDS epidemic in the making. Non-government organizations are playing a lead role in efforts to prevent and control the spread of the HIV virus, and the government is investing in the physical infrastructure required to test for the virus and to protect the blood supply from being contaminated.

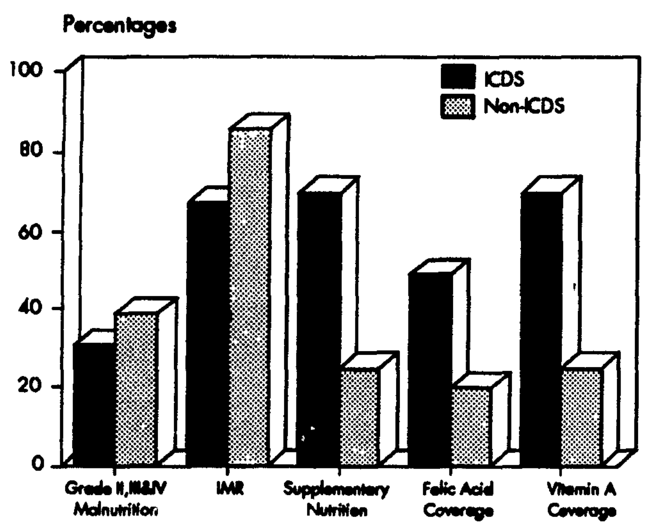
USAID will assist with these efforts through supporting NGO programs that have a significant impact on the spread of AIDS. Such programs will encourage the use of condoms, treatment of sexually transmitted diseases, and the reduction of sexual partners.

Decreased Level of Malnutrition

Poverty and malnutrition remain a serious problem for a large percentage of India's population. The Mission plans to continue its large Title II program managed by CARE and CRS to decrease the level of malnutrition in high-risk groups. We expect CARE to continue its association with the Integrated Child Development Services (ICDS) program, with its emphasis on reaching high-risk children and pregnant and lactating mothers with food supplements, nutrition education and primary health care. A consolidated CRS program will continue to provide food supplements to India's most disadvantaged groups.

With strong AID support, CARE is collaborating with the Government of India in the most ambitious Primary Health CARE/Child Survival Program in the world. The Integrated Child Development Services (ICDS) provides, on a daily basis, food, nutrition education, and basic health services to more than 17 million young children (0-6 years old) and 6.1 million pregnant and lactating mothers. Of this total, USAID, through CARE, assists over 7 million women and children. This activity represents the most significant component of the Mission's Title II program which, at an annual commodity level in excess of $70 million, is the largest in the world. As indicated below, the ICDS program has had significant nutritional and health impacts at the village level.

Impact of ICDS Nutrition Services : Some Indicators



Source : ICDS - Evaluation and Research 1975-1988

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PROGRAM INDICATORS

1. Increased Contraceptive Use:

The prevalence of contraceptive use is a significant determinant of the birth rate. The choice of contraceptives, or the method mix, is also a very important determinant of the impact of the program. The more methods of contraception available, the higher the prevalence rates. Our aim will be to increase the prevalence of contraceptive use and to increase the number of families using spacing methods.

2. Increase in the number of families receiving health and family planning services from non government sources:

The Indian Government has recently recognized the importance of involving non government organizations in the delivery of health and family planning services. USAID has played an important role in encouraging this change in attitude and has provided assistance for demonstration projects. The present challenge is to broaden NGO participation so that large numbers of families receive services from the private sector.

3. Decreased Incidence of Malnutrition:

Chronic malnutrition is perhaps the worst scourge of poverty, frequently condemning the children of poor families to low-paying menial work in their productive years. Several programs exist to help alleviate these conditions. Through our large Title II program, we hope to help reduce third and fourth-degree malnutrition in the target populations.

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SPECIAL THEMES FOR THE 1990s

The Agency for International Development has identified five major programmatic themes to enhance its contributions to international development in the 1990s. These themes include democracy, family and development, environment, business and development, and sustainability. With India's well entrenched democratic values buttressed by a free press, a strong and independent judiciary and a multi-party political system, the Mission has not identified support for democracy as a critical element of our assistance to India. The other programmatic themes, however, are important components of USAID's program for the 1990s. New initiatives in these areas are summarized below.

THE ENVIRONMENTAL PARTNERSHIP

The US-Asia Environmental Partnership (US-AEP) is a Presidential initiative aimed at bringing together the American business community, government agencies, and private organizations in a long-term collaboration with Asian counterparts. The Partnership is based on the premise that continued economic and social progress and increased environmental protection in the region are mutually beneficial. The initiative further posits that the roles of private citizens, businesses and governments in sharing responsibility and financing for this partnership are the key to its success, and tremendous opportunities exist for such mutually beneficial collaborations.

All three of the Mission's program objectives are consistent with the larger aims of the Environmental Alliance initiative. USAID/India already has in place programs that will help translate US-AEP ideals into concrete realities. Areas of Mission involvement explicitly linked to the goals of the US-AEP include energy efficiency and conservation, and preservation of bio-diversity. New initiatives are planned to promote Indo-U.S. commercial ties related to environmental services and technologies.

Energy Efficiency and Conservation: Of the 50 major cities around the world monitored by the U.N. Global Environment Monitoring System, New Delhi

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❑ Increased Contraceptive Prevalence

The government's traditional approach to family planning, emphasizing terminal methods and target setting, has failed to keep pace with tremendous advances in contraceptive development and demand generation made over the past two decades. While the aggressive sterilization campaigns of the early 1970s have subsided, the national family planning program's image still remains tarnished and lacks broad community support. Many Indians view family planning as the "duty" of a good citizen, rather than as a means to enhance the health and well-being of the family.

From all indications, the potential for positive change is greater now than at any time in the past. Faced with a population crisis every bit as serious as its economic crisis, the Government is currently reevaluating its approach. In addition to advocating the use of birth spacing methods to encourage the participation of young couples in the program, it is also promoting a greatly expanded role for non-governmental organizations (NGOs) and the corporate sector in service provision. The government also plans to place much greater emphasis on new contraceptive technologies and experiment with such service outreach approaches as community-based distribution and social marketing, which have been proven successful in other settings.

The Government also recognizes that an intensive family planning effort is required in the four large northern Hindi-speaking states of Bihar, Madhya Pradesh, Rajasthan and Uttar Pradesh. These states have the highest population growth rate in India, with a total fertility rate of 5.7 compared to the Indian average of 4.3. Not too surprisingly, the family planning program performance has been weakest in this region. The effective couple protection rate of these four states is approximately 24 percent, while the southern states, such as Kerala and Tamil Nadu, have averaged 47 percent and 40 percent respectively. A reduction in India's rapid population growth will not be realized until fertility decreases in these northern states.

The centerpiece of the Mission's strategy to promote smaller, healthier families will be a new effort to help establish a modern family planning program in Uttar Pradesh, India's largest state with over 140 million people. Emphasis will be on:

- Access to and quality of family planning services.
- Communication strategies to increase knowledge of available contraceptive methods and to promote informed choice in the selection of a specific method.

ranks first in the level of air pollution, Calcutta fourth and Bombay tenth. The major cause of air pollution in India is coal-fired electric power generation. A study commissioned by the Mission estimates that improved energy efficiency of thermal power plants and major industrial consumers could reduce air pollution by as much as 15 to 20 percent.

The Mission is supporting a number of initiatives to encourage such improvements. The Alternative Energy Resources Development Project is currently developing technologies to reduce NOx emissions from coal-fired electrical power plants. The Program for Accelerated Commercial Energy Research is developing commercially attractive methods for utilizing biomass and solar energy. The Energy Management Consultation and Training Project will soon make available to India's major industrial consumers private U.S. energy audit services to enable them to reduce energy consumption. All of these projects have strong linkages to U.S. businesses, environmental organizations and trade and industry groups, and will provide opportunities to demonstrate energy efficiency and conservation technologies.

Preservation of Bio-Diversity: India's biological diversity is among the most varied in the world and includes both domesticated crops and their wild relatives. The Mission is involved in a unique effort to help India preserve its rich endowment of plant germplasm and to make it available for international crop-improvement research and other commercial as well as public bio-technology needs. The National Bureau of Plant Genetic Resources (NBPGR) is responsible for the conservation of India's plant germplasm, and, through its Plant Genetic Resources Project, the Mission is helping to strengthen NBPGR capabilities. Efforts include financial support for a new National Gene Bank; joint Indo-U.S. germplasm exploration and collection programs; and a comprehensive inventory of the 100 plus germplasm collections in India. The aim of this unique effort is to help India preserve its rich endowment of plant germplasm and to make it available for international crop improvement research as well for commercial development.

Trade in Environmental Services and Technologies (TEST): India's haphazard industrial development has had devastating effects on its environment. Some of India's greatest rivers are biologically dead and chemically lethal. Air quality in urban areas is among the worst in the world. Problems associated with the disposal of hazardous waste are just beginning to emerge and are potentially quite serious. Limited access to environmental services and technologies seriously impedes India's ability to address these severe problems. The U.S. has made significant progress in addressing similar environmental concerns and, in the process, has developed a renowned environmental service sector. The U.S. has also learned to create incentives for voluntary industry compliance with environmental standards.

The Mission is currently designing an innovative program, known as TEST, to increase the competitiveness of Indian enterprises while mitigating negative environmental impacts. USAID will facilitate the ability of these firms to access commercial environmental services and technologies available in the U.S. and will facilitate the establishment of commercial Indo-U.S. joint ventures for this objective. The program will also offer cost-beneficial alternatives to encourage voluntary compliance with India's increasingly rigorous environmental standards.

TEST will provide a vehicle for implementing the Environmental Partnership in India and will, we believe, provide many useful lessons for other Missions beginning to consider how they might best support this new initiative. While merging with USAID objectives, TEST will advance the goal of sustainable development by responding to India's need for environmentally friendly technologies. TEST will also encourage Indo-U.S. trade in an area of high industrial demand and growing U.S. capability. Finally, TEST will help create a broad and dynamic marketplace for environmental services and technologies in India while expanding the private sector role in economic growth.

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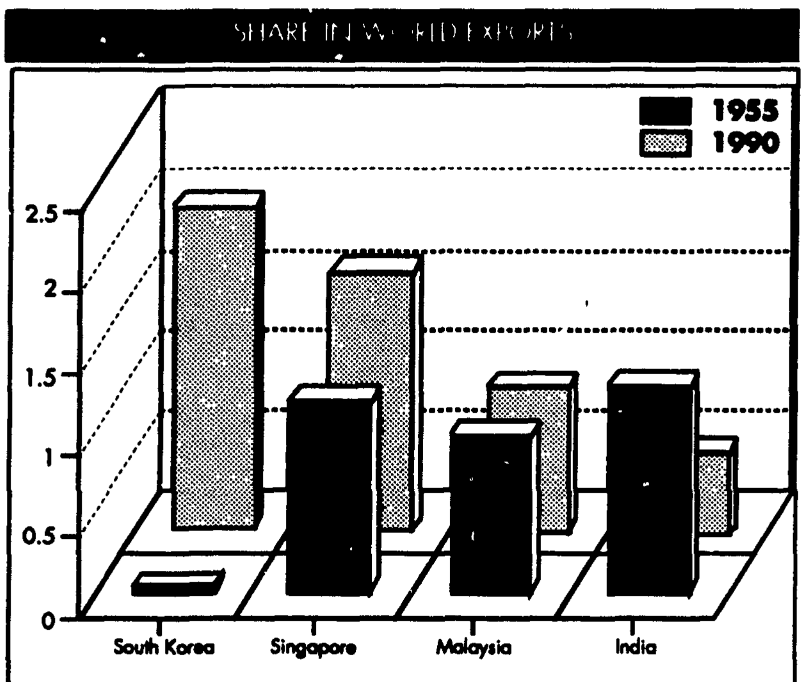
EXPANDED COMMERCIAL TIES

USAID has a double stake in the globalization of trade and investment. As a development agency, we have an interest in assisting local enterprises become more competitive as domestic producers and global exporters. As an agency of the U.S. government, we have a stake in promoting participation of U.S. firms in activities that support sustainable growth in developing economies.

One dramatic change that will result from liberalization measures will be India's rapid integration with the world economy. India's current level of trade with the outside world is of little significance. The same is true of foreign investment in India. In 1990, for example, India attracted $425 million dollars in foreign direct investment. Thailand, by comparison, received over $1.8 billion, while Malaysia attracted nearly $3 billion. With many of the critical ingredients necessary for rapid economic transformation, India, too, can become a major player in the global economy.



Source : CMIE 91 Vol. 1

The U.S. stands to gain from India's shift to an outward orientation in its pursuit of accelerated economic growth. The U.S. is already India's largest trading partner and, with a large population of resident Indians and strong academic and scientific links between the two nations, the U.S. is certain to benefit from India's integration with the world economy. In the brief period of recent liberalization, a number of major U.S. corporations have decided to invest in the new Indian economy.

Since the mid 1980s, USAID has advocated a more significant role for the private sector in India's development. An important component of Mission activities has been to promote a new partnership between Indian and U.S. business. Over the past five years, we have helped establish over thirty

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Indo-U.S. joint business ventures in such diverse areas as information technology, energy, agribusiness and biotechnology.

In the future, our program will place an increased emphasis on strengthening Indo-U.S. commercial ties. New efforts will focus on environmental services and technologies, discussed in the preceding section on the environmental partnerships, agribusiness, and financial services. At present, efforts in the financial services are primarily focussed on the housing finance system and the capital markets. New plans include assessing opportunities for providing increased assistance to the commercial banking sector.

U.S. AND INDIA : PARTNERS IN AGRIBUSINESS

Giorgio, a leading U.S. mushroom processor facing fierce competition from producers in the People's Republic of China, began searching for low cost mushroom supplies in the developing world. In 1986, Giorgio entered into a joint venture with Ponds of India to develop a production package suitable for large-scale button mushroom production using non-traditional feed stock. With USAID support, the partners established a pilot plant of 120 TPA capacity consisting of seven growing rooms, a small analytical lab, and facilities for producing casing materials. Consignments shipped to the U.S. passed Giorgio's quality testing, and also gained U.S. FDA approval. Ponds has now put up a 3000 TPA facility and plans to expand its commercial production to 10,000 TPA by the year 2000. The commercialization of this project has resulted in substantial savings in the cost of mushrooms to Giorgio and has consequently increased sales and market shares. For Giorgio it has been a successful test effort to establish a long-term supply agreement with a firm in a country with low labor costs.

Another opportunity for strengthened commercial ties between the U.S. and India concerns energy efficiency technologies. A study commissioned by the Mission indicates there will be a large market for energy efficiency technologies in India in the coming decade. Current projections of demand range from $15 billion to $25 billion. The U.S. dominates the world market in the manufacture of energy efficient equipment, including cogeneration technologies. The U.S. also has a large energy service industry that stands to benefit from expanded opportunities in India that will result from increased investment in energy efficient technologies.

Finally, the Mission plans to promote joint efforts of private business, trade, and industrial associations in India and the United States to assist in restructuring Indian enterprises.

A SUSTAINABLE DEVELOPMENT PARTNERSHIP

In the coming year, USAID intends to explore the possibility of facilitating the creation of a private foundation to fund Indo-U.S. development initiatives to complement our new program strategy. A private development foundation would have many advantages over its government counterpart and, less encumbered by regulations, could respond quickly to development opportunities. Towards the end of the decade the new foundation could also become the focal point of efforts to sustain long-term, mutually beneficial ties between U.S. and Indian development organizations.

We plan to encourage and assist a prestigious private American foundation to take the lead in forming a small consortium of organizations to establish a private American presence in India. Ideally, the foundation would be created under an agreement between the U.S. sponsoring organizations and the GOI, with the broad mandate of promoting economic cooperation between the two countries. The foundation would fund research and educational exchanges, and sponsor seminars and workshops on issues of mutual concern. The initial focus would be on agriculture and natural resource management areas where substantial U.S. investment has recently concluded, but where there is significant potential for supporting linkages between U.S. and Indian institutions. Over time, the foundation would expand its agenda.

USAID plans to begin by providing a planning grant to an American foundation to help develop a strategy for the consortium in the U.S. and to establish a foundation in India. USAID would from time to time contract with the foundation to carry out special activities, and contributions would also be sought from the private sector. Once the foundation is financially and programmatically viable, we would be in a better position to propose to Congress that the USG contribute to the foundation.

VII

PROGRAM MANAGEMENT

The current year is a time of transition for USAID/New Delhi. A substantial number of projects begun in the early 1980s, including the large irrigation and social forestry projects, will come to an end. USDH levels drop another two positions to 15, down from 26 in 1987. While the reform measures in India will create many new opportunities for USAID assistance, staffing and operating expense levels continue to seriously limit the types of programs the Mission can effectively manage. The Mission has already taken a number of steps in response to India's changing environment. These steps include the following:

1. **Concentration of the Portfolio on Three Program Objectives:** The USAID program represents less than one half of one percent of donor assistance to India. This statistic underscores the necessity to focus USAID's resources on a limited number of programs to ensure the quality of each component. Based on our goal of accelerating broad-based market-led growth, the Mission has identified three program objectives which have been described in sections III, IV, and V of this document. As a consequence of the decision to focus assistance in these three areas, certain elements of the existing portfolio will be phased out in a manner that ensures the sustainability of their achievements.

   Eight on-going projects related to agriculture research and education, natural resource management, and biomedical research will be among the discontinued programs. By the end of FY 93, the Mission will have only two projects, Plant Genetic Resources and Quality Control of Health Technologies, that are not directly supportive of the three program objectives. The Plant Genetic Resources project offers a unique opportunity to contribute to the global effort to support biological diversity, and will be continued until its completion date of September 30, 1995. The Quality Control of Health Technologies project is essential for establishing the government's capability to ensure quality control of biologicals and surveillance of the AIDS virus. The project is also a key component in ensuring responsible private sector participation in the health care field. The Mission is collaborating with the Japanese, on this activity, and plans to support the project until its completion date of September 30, 1998.

2. **Reduction in the Number of Implementation Units:** Many projects in the current portfolio have a large number of implementation units that require oversight by Mission staff. The Water Resources Management and Training Project, for example, involves management oversight for 27 different in-country institutions. New projects are being designed in a way that significantly reduces management intensity and scales back the number of implementation units. Agriculture Commercialization and Enterprise (ACE), and the new AIDS Prevention and Control, TEST, and Innovations in Family Planning Projects, will each focus on one state and operate through a limited number of project management units.

3. **More Efficient Use of Agency Resources:** USAID wastes a considerable amount of time and energy moving money around within the organisation. Last year, nearly one-third of the Agency's population funds went first to Missions abroad, then back to Washington, where contracts were signed for goods and services to be provided to the Missions. We are collaborating with the R&D Bureau to simplify the "buy-in" process for our new family planning and AIDS initiatives by requesting that funds required for purchase of AID/W services remain in Washington and be provided to the Mission on an "in-kind" basis. This procedure will also simplify our negotiations with the Government on technical assistance and other offshore costs required to achieve project objectives.

4. **Greater Emphasis on Performance and Accountability:** Mission efforts to focus program resources will be accompanied by a series of related initiatives that promote results in the management of the portfolio. Key to these initiatives will be an expanded Program Performance Information System (PPIS) that routinely tracks progress toward achievement of the Mission's three program objectives. Finalization of the main performance indicators and identification of annual progress benchmarks will take place followng review of the strategy and will also occur in coordination with CDIE efforts associated with the new PRISM activity. In addition to PPIS activities, Mission attention to results will be fostered through continued emphasis on high calibre evaluations that critically examine the achievement of project objectives. Lastly, the Mission is in the process of modifying its performance award and incentive systems for all personnel in order to

recognize those employees whose efforts are making a difference in progress toward the achievement of the three program objectives and doing so in a cost-effective and financially accountable manner.

Resource Levels : The Mission recently received approval for a $50 million two year PL 480 Title III program to support India's dramatic shift in policy direction. We are currently engaged in the design of a major family planning project and are proceeding on the basis that an additional $20 million will be transferred to our OYB each year and another $10 million annual "in-kind contributions" will be provided by the R&D Bureau for this effort. Allocation of Mission financial resources for the coming five years is described in the accompanying table.

In conjunction with the preparation of this strategy, Mission management carried out an intensive review of USDH and FSN staffing patterns. As a result of this effort, staff positions were realigned to support new initiatives such as TEST, Title III and family planning programs. We also concluded that many of the new skills are available in India and we are now in the process of actively recruiting local staff in such areas as financial markets and business services to meet our new needs.

At the same time, USDH staffing levels impose the single most binding constraint to new development initiatives supportive of the three program objectives. Under the current staffing levels, for example, we will have to forego : 1) a new Housing Guaranty Program aimed at introducing cost recovery mechanisms for construction and maintenance of municipal infrastructure; and 2) additional efforts to encourage Indo-U.S. trade and investment, including greater support for U.S. Asian Environmental Partnership (AEP).

Donor Coordination: The Mission has close working relationships with the donor community in India, based primarily upon individual contacts in areas of mutual interest. In a number of fields, such as the energy sector, Mission projects are managed in close collaboration with India's largest donors including the World Bank, the Asian Development Bank and Japanese OECF. We will continue to place a high priority on collaboration with other donors in our new initiatives, matching our in-country presence and access to top quality technical resources with their large financial contributions.

PROPOSED INVESTMENT PLAN

(in million dollars)

Program Objectives/ Active Bilateral Projects	PACD	OBLIGATIONS Thru FY 91	FY 92	FY 93	FY 94	FY 95	FY 96	FY 97
Improved Financial and Regulatory Environment								
1. Development & Management Training		9.48	0	0	0	0	0	0
2. Technical Assistance & Support Project	30-Sep-96	9.57	3.00	1.50	2.93	3.00	0	0
3. Housing Finance System Expansion Prog	30-Sep-96	0	1.00	1.00	1.30	1.00	0	0
4. Financial Institutions Reform	30-Sep-0	0	0	0	2.00	2.00	3.00	2.00
5. Housing Guarantee Program	n/a	180.40	25.00	25.00	0	0	0	0
6. *PL 480 Title III*	*n/a*	*0*	*17.00*	*17.00*	*17.00*	*17.00*	*0*	*0*
Subtotal		199.45	46.00	44.50	23.23	23.00	3.00	2.00
Increased Productivity of Indian Enterprises								
7. Prog. for Acceleration of Comm. Energy Res.	30-Jun-96	10.00	0	2.00	2.00	2.00	2.00	2.00
8. Prog. for the Advancement of Comm. Tech.	31-Jul-95	16.74	5.00	0	0.99	0	0	0
9. Center for Technology Development	31-Jul-95	5.00	0.00	1.00	1.50	2.50	0	0
10. Energy Mgt. Consultation & Training	31-Mar-97	4.00	1.00	1.00	1.50	2.50	3.00	4.00
11. Agricultural Commercialization & Enterprise	30-Sep-98	5.00	2.30	0	2.20	2.00	3.00	2.00
12. Trade in Env. Services & Technologies	30-Sep-99	0	3.00	2.00	2.00	2.00	5.00	5.00
13. Restructuring of Enterprises & Trade	30-Sep-98	0	0	1.50	2.00	4.00	5.00	6.00
14. *PL 480 Title III*	*n/a*	*0*	*8.00*	*8.00*	*8.00*	*8.00*	*0*	*0*
Subtotal		40.74	19.30	15.50	20.19	23.00	18.00	19.00
Smaller, Healthier Families								
15. Family Planning Communcations & Mktg.	31-Mar-93	23.72	0	0	0	0	0	0
16. Private Vol. Organizations for Health-II	30-Sep-95	6.80	2.20	0	1.00	0	0	0
17. AIDS Prevention and Control	30-Sep-97	0	2.00	1.00	1.00	2.00	2.00	2.00
18. Innovations in Family Planning Services	30-Sep-02	0	22.50	31.00	20.00	20.00	20.00	20.00
19. PL 480 Title II	n/a	n/a	77.18	80.02	80.00	80.00	80.00	80.00
Subtotal		30.52	103.88	112.02	102.00	102.00	102.00	102.00
Projects not Contributing to the above Objectives, but are Important to Continue								
20. Plant Genetic Resources	30-Sep-95	10.20	0	2.00	2.50	0	0	0
21. Quality Control of Health Technologies	30-Sep-98	5.00	0	0	2.30	2.00	2.00	2.00
Subtotal		15.20	0	2.00	4.80	2.00	2.00	2.00
TOTAL PROJECTED DA		105.51	42.00	44.00	45.22	45.00	45.00	45.00
TOTAL PROJECTED NON-DA		180.40	127.18	130.02	105.00	105.00	80.00	80.00

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POLICY REFORMS AND THE NEW ECONOMIC ORDER

INTRODUCTION

In mid-1991 the Government of India announced a series of bold initiatives aimed at ending the country's 40 years of isolation from the global economy. In the face of tumbling international credit ratings and near foreign exchange bankruptcy, these radical reforms were designed to move India away from state-led economic development by deregulating industry, liberalizing foreign trade and investment, and substantially reforming fiscal policies.

These reforms were instituted by the minority government which came to power in June 1991, and have received the tacit backing of the main opposition party. Most observers agree that the changes point to an irreversible new direction in Indian policy, but will need additional measures and disciplined implementation in order to fully succeed. The March 1992 budget presentation and the recently announced Import-Export Policy reaffirm the government's commitment to policy reforms that add momentum to the process begun last summer.

The policy reform package has focused on achieving three main objectives: restoring macro-economic stability and regaining the nation's favorable international credit rating; opening the economy to global competition; and significantly reducing the role played by India's public sector in the economy. Deregulation of trade, industry, and finance are the centerpieces of these closely connected initiatives.

ECONOMIC CRISIS

Over the past 40 years, state-led economic development in India has resulted in a high-cost economy characterized by massive poverty and unemployment, economy-wide inefficiencies, and chronic foreign exchange shortages. Throughout the 1980s, India's economy came under increasing pressure as a result of its misdirected policies. The government responded to the worsening situation with limited reform measures and large scale borrowing from abroad.

The deteriorating situation reached crisis proportions in mid-1991 as foreign exchange reserves dwindled to only fourteen days worth of imports. International credit rating agencies sharply downgraded the country's status. Short-term credits became difficult to obtain, and Non-Resident Indian (NRI) hard currency banking deposits fell sharply. The near depletion of foreign exchange reserves resulted in widespread shortages of essential imported commodities and cutbacks in industrial output, both of which fueled inflationary pressures. The crisis left India with few options regarding the future course of its economic development.

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STABILIZATION

Faced with perhaps the country's most serious economic crisis since independence, the newly elected government headed by P.V. Narasimha Rao took immediate action after coming to office in June 1991 and announced a series of economic reforms. Initial attention focused on restoring macro-economic stability. The rupee was devalued by 20 percent to prevent the flight of NRI money and to make Indian exports more attractive. The FY 91/92 budget curbed government expenditures and included measures to augment public revenues. The budget also cut the fertilizer subsidy, which was one of the largest federal expenditures, and called for plans to sell government equity in selected public sector undertakings.

The FY 92/93 budget proposals, effective April 1, demonstrated the government's continuing determination to achieve macro-economic stability. The rupee was made partially convertible effectively devaluing it by an additional 15 percent. The budget also called for: additional cuts in public expenditures; a significant reduction in tax rates while broadening the tax base; and increases in railway and bus fares as well as the prices of steel, coal, petroleum and other key commodities.

POLICY REFORM

When the new government announced steps to restore macro-economic stability, it also introduced a series of sweeping economic reforms. These reforms abolished many of the highly restrictive regulations on industry and commerce, and represent a significant move toward the market orientation that will help India integrate with the world economy. Trade, industry, and finance have been identified as the areas most in need of reform. Highlights of the changes are described below.

A. Trade

Foreign trade policies over the past 40 years deliberately isolated India from the rest of the world. High import tariffs, quantitative restrictions on certain commodities and an over-valued rupee produced a highly protected economy. The relatively little trade that did take place included large barter transactions with Eastern Europe and the former Soviet Union.

In its first nine months in office the Rao government took several steps to end India's isolation and help domestic enterprises become internationally competitive. Devaluation of the rupee was key in these efforts.

The new five year trade policy, effective April 1, 1992, has abolished import and export licensing and discretionary controls for all capital goods, raw materials and spare parts except for two short negative lists. As a result, quantitative restrictions on imports have been drastically reduced. Import duties have been substantially reduced on capital and agricultural goods, with peak tariff lowered from 150 percent to 110 percent and from 80 percent to 55 percent on project imports and general machinery. Tariff on import of capital goods is likely to be reduced further when budget proposals are passed by the Parliament.

The government also announced several measures to encourage direct foreign investment. It has increased the ceiling on foreign equity holding to 51 percent in 34 industry groups, and in the power sector up to 100 percent foreign ownership with full repatriation of profits. The government modified the highly restrictive Foreign Exchange Regulations Act (FERA) allowing FERA companies (foreign firms with equity holdings of 40 percent or more) to borrow money and accept deposits in India, deal in immovable property, and use of trademarks. A Foreign Investment Promotion Board (FIPB) has been established to expedite clearances for new investments.

B. Industry

For decades, India's industrial policies have promoted import substitution, discouraged competition, favored state-owned enterprises, and tightly regulated the operations of privately owned firms. As a result, Indian firms use outmoded technologies to produce high-cost goods of inferior quality. Incremental liberalization measures introduced in the mid-1980s demonstrated the potential benefits that could result from dismantling restraints on internal competition, and the crisis of mid-1991 highlighted the need for an even greater overhaul of industrial policies.

The Rao government instituted major changes in India's industrial policies. Industrial licensing has been abolished except for a short list of "strategic" industries. The Monopolies and Restrictive Trade Practices (MRTP) Act was amended to eliminate the need for government approval to expand or diversify operations and the number of areas formerly reserved for the public sector has been narrowed significantly from seventeen to eight. In addition the government has begun the process of disinvesting in state owned enterprises by selling equity to the public.

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C. *Finance*

Shortly after taking office the government established a high-level commission to examine the country's financial sector and to recommend policy changes. In December 1991 the commission issued a report that included several highly critical findings.

The report notes that the variety of institutions and instruments in the financial sector has greatly [illegible]ified, but the rate of return on these instruments has been very [illegible]. It attributed the poor performance to regulations and excessive political interference in credit allocations. The commercial banking sector, for instance, is close to insolvency due to the large number of forced loans provided at concessional interest rates to enterprises engaged in activities favored by government planners. Capital markets have also been hampered by strict government regulations.

Since release of the report, the government has announced some measures that begin to address the problems identified by the commission. It will now be possible for the private sector to set up commercial banks and for foreign banks to expand their operations in India. The government has proposed the gradual elimination of subsidized interest rates for specified priority sectors and removed interest rate restrictions on debentures and public sector bonds. Similar steps are being taken to facilitate development of the capital market. The new budget proposes to eliminate several controls over capital issues including setting the selling price for new issues. At the same time, the statutory powers of the Securities and Exchange Board of India (SEBI) have been enhanced to safeguard investor interests.

REDEFINED ROLE OF GOVERNMENT

The Government of India plays a dominant role in the country's economy. Three out of every four workers in the formal sector, over 24 million people, are employed by the government. Through licensing and other regulatory controls, the government is involved in virtually every facet of the business operations of privately owned firms. The government's pre-eminent role in the economy is also ensured by the large number of state-owned enterprises that monopolize key industries. The reforms announced by the Rao government redefine the government's role in the economy. The majority of industries previously reserved for state-owned enterprises have now been opened up to private sector firms. Railways, the largest government organization, now welcomes private sector investment. Private sector participation in highway development is also encouraged. Several of the large, state-owned enterprises will soon be offering shares on stock exchanges, contributing to a gradual shift to private ownership of these operations.

Delicensing and deregulation measures have also diminished the role of the government. Several public agencies responsible for issuing licenses are being reorganized and may eventually be closed. The government is discussing steps to reduce its number of employees with a tentative ten percent reduction mentioned as a target for the coming year. Senior officials have issued notifications that decisions must now be made within given timeframes, and officials are being encouraged to meet with representatives outside of government to find quick solutions to problems. Transparency in decision-making is also being stressed. The message to the bureaucrats is loud and clear – support the reforms and act as facilitators rather than regulators.

RESULTS TO DATE

The Rao government's reform program is less than one year old, and it is clearly too soon to draw definitive conclusions about these dramatic changes. Initial returns are in, however, and the results are encouraging.

One of the most promising changes so far is that official foreign exchange reserves have increased almost four-fold, up from the $1.2 billion level of June 1991 to the present level of approximately $5.0 billion. The fiscal deficit has also dropped sharply from 8.4 percent to 6.3 percent of GDP.

Although the tangible impact of trade reforms, particularly import liberalization, will only become visible over time, some significant changes can already be seen. Exports to hard currency areas are rising as India's trade deficit in the first ten months of 1992 declined by $3.86 billion, though much of this was attributable to curbs on imports. Direct foreign investment is on the rise as the government has demonstrated a firm commitment to expediting proposals.

Although industrial production growth in FY 92 is likely to slow substantially, primarily as the result of import compression, the more favorable policy environment should set the stage for a significant upturn in industrial growth in 1993. The bullish stock market and the substantial amounts of unaccounted "black" money now being channeled into the economy reflect a highly optimistic outlook on the part of many Indian investors.

NEXT STEPS AND CONCLUSIONS

These early results indicate better economic performance is within reach, as are better living and working conditions for India's poor. Improvements in the foreign exchange situation should make it possible for the rupee to be fully convertible and the foreign direct investment limit of 51 percent could soon be abolished. Still, additional reforms are needed. Weak protection of intellectual property rights and poor banking services continue to inhibit investment, and further liberalization measures must be realized in the financial sector.

One area vital to the success of the entire liberalization package is an "exit policy" – a program to close down sick or unviable enterprises. The GOI has announced its commitment to an exit policy, but has been hesitant to act given the political sensitivity of the subject. Still, the GOI has made clear commitments to set up a National Renewal Fund (NRF) with a substantial corpus of about Rs.2.0 billion in the first year. The main objective of the fund will be to provide a social safety net to protect workers from the adverse consequences of the country's economic renewal. The NRF will develop financial compensation packages for workers who lose jobs and will provide programs to retrain and redeploy them. Industries and state governments are expected to participate as partners in this venture. USAID has proposed a $50 million Title III program to supplement GOI efforts.

There is no question that the economic policy reforms instituted by the Rao government are historic in nature. India has shifted from the pervasive system of state intervention and economic controls to comprehensive deregulation of industry, liberalization of foreign trade and direct investment, and significant financial sector reforms. The federal budget for FY 92/93 reflects a strong commitment to continue the reform program.

USAID / INDIA STRATEGIC FRAMEWORK, FY 1992 - 2000
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PROGRAM DOCUMENT

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