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Strengthening Free Enterprise in India: RBI Governor

"India has come a long way in encouraging free enterprise - from tiny shops to large internet start-ups, the spirit of entrepreneurship is alive. Doing business is now more reputable than just a few decades ago, as is getting rich. Graduates increasingly want to start businesses or work for start-ups rather than join an established consultancy or a bank. What was now needed was to continue improving the environment so that everyone had a better chance." This was stated by Dr. Raghuram Rajan, Governor, Reserve Bank of India on May 21, 2016 while addressing ministers, bureaucrats and bankers at the fourth Knowledge Hub organised by the State Government in Bhubaneswar, Odisha.

In his lecture, the Governor focused on how far has India come in building a start-up environment but said there was some still way to go. Starting with historical three conditions for free enterprise to flourish, namely, i) Level playing field with easy entry and exit; ii) Access to input and output markets; and iii) Protection of property rights, the Governor added two more for them to be politically viable, namely, i) broadening access to capabilities and ii) a basic safety net.

Dr Rajan pointed out that India started doing away with the Licence/Permit Raj in the 1990s, and opened up business to entry and competition. Recently, the government has moved to transparently auctioning resources like spectrum and coal mines, thus ending the monopoly of a few over resources, that could have been termed the Resource Raj. The government has reduced the Inspector Raj by doing away with a number of entry barriers for start ups, he said, quoting the example of Prime Minister's initiative on compliance based on self certification through a mobile app, the move in the Union Budget to reduce regulatory burden for startups with no inspection to be conducted in certain areas for three years; and self-certified compliance with environment laws for startups under 'white' category.

The Governor also spoke about finance which was weighted against new and untried firms the world over. However, by targeting priority sector norms specifically at micro and small enterprises, while also including medium enterprises, banks have been able to show significant improvement in lending to this sector. Loans extended by public sector banks to small and medium enterprises under priority sector norms, for instance, have gone up from Rs. 4 lakh crore as at end March 2012 to Rs. 7 lakh crore as at end March 2015. Performance of private sector banks is even better having risen from Rs. 109 thousand crore to Rs. 232 thousand crore in the same period. The outstanding credit to medium and small enterprises thus has grown 6% of GDP to 7.7% of GDP between 2012 and 2015. VC/PE funding has increased 22 times from \$ 250 million in 2011 to \$ 5500 million in 2015. The Governor described

other ways in which the government and the Reserve Bank have taken initiatives to ease small business financing.

Going forward, the Governor stated that there were some continuing infirmities that especially hurt new firms, such as, infrastructure and logistics, which he said were weighted against the small. Similarly, difficulties in land acquisition were also weighted against the new. However, there was competition between states to reform these laws. Further, progress on resolving distress quickly, such as, enactment of the new bankruptcy code, would help assure a clean exit to firms that failed, and a redeployment of their resources in more useful ways.

Pointing out that the government had delivered on prescribing moderate and predictable taxes generally, and granting income tax exemption for 3 years as also on capital gains for startups, the Governor said that now what was necessary was to reduce any remaining uncertainty about tax demands and automation of significant parts of the tax process.

The Governor stated that it was necessary to broaden access to capabilities by providing decent education and health to individuals. "Aam aadmi attaches no value to free enterprise if he cannot participate by getting a job or starting a firm," he said. The Skill India programme of the government was rightly directed towards imparting needed skills, including vocational training, he pointed out. In addition, the Governor argued that we should ensure a basic affordable safety net for individuals – unemployment insurance, basic health care and old age pensions. "If insurance is not explicitly provided up front, it will be implicit in a democratic society," he said and added that safety net can also encourage people to take risks which they would shy away from otherwise.

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