BOMBAY FIRST

Mumbai as an International Financial Centre - A Roadmap

BOMBAY first

a corporate initiative to rejuvenate mumbai

FOREWORD

The mission of Bombay First is to make Mumbai a better place to live, work and invest in. The expert committees of Bombay First have endeavonred to fulfil this mission over the years. Right from its inception, Bombay First has been advocating the case of Mumbai as an International Financial and Services Centre.

The process of economic reforms and globalisation will have significant impact on Mumbai and will require the city to specialise in areas that it has comparative advantages in. The Bombay Chamber of Commerce and Industry organised a seminar on "Bombay – the Emerging Global Financial Centre" in February 1994. The seminar included four focus sessions, namely, Housing and Social Infrastructure, Financial Sector, Telecommunications and Transport. During the discussions, many ground realities about Bombay came to the fore and also some excellent suggestions to make Bombay a global financial centre. The decision to establish Bombay First and the BCPRF emanated from this seminar.

In 1999, the Financial Services Committee of Bombay First, headed by Dr. R.H. Patil, MD, National Stock Exchange Limited, commissioned CRISIL Advisory Services to carry out an indepth study, titled "Mumbai as an International Financial Centre – A Roadmap". This study has already elicited great interest in various quarters.

The recommendations of the study have already been presented to the Chief Minister, Government of Maharashtra, the Chief Secretary's office and other senior Government officials.

I wish to record our sincere appreciation for the financial support received from EXIM Bank and HDFC and the Bombay City Policy Research Foundation.

On behalf of Bombay First and our sponsors, it gives me great pleasure to present this report to the city of Mumbai.

Mumbai
December 2000

K.K. Nohria
Chairman, Bombay First

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EXECUTIVE SUMMARY

1.1. Background

Bombay First, as a part of its activities to promote the cause of Mumbai, has invited CRISIL to prepare a roadmap for developing Mumbai as an International Financial Centre Bombay First is an initiative of the corporate houses associated with the Bombay Chamber of Commerce and Industry. It was set up with the vision to help improve the economic and the social infrastructure of the city and to improve the quality of life of its citizens. The deliverables included a report covering the evolution of financial centres, the forces that contribute to their success, the positioning of other regional financial centres, USP and niche areas for Mumbai, types of financial services to be provided, a summary of regulatory changes and steps for market development. The deliverables also included the identification of hard and soft infrastructure requirements for the development of the financial centre. The study was divided into two modules:

Module	Focus Area
Module I	Survey of regional financial centres
Module II	Development of the road map

1.2. Introduction

An international financial centre provides specialised financial services on a global scale. The international financial centre status brings about international prominence, remarkable employment opportunities and a transformation to a high value, service based economy. As a result the network of financial centres is expanding, with many contenders vying for a large share of global financial services pie.

Few cities can aspire to become a financial centre of the magnitude of London or New York. However some locations are blessed with advantages that put them in a superior position to evolve into a financial centre. Mumbai is one such centre, having already established its position as the financial capital of India. Mumbai's advantages are that it has a large population of highly skilled English speaking workers and a reputation for attracting the best managerial talent in India. However, it is important that Mumbai gears itself to retain a large volume of the potentially high value financial activity that India offers and also from the Asian region.

Every national financial capital in the Asian region has attempted to attract top international corporate headquarters to their main cities. One of the main reasons is that financial centres attract high volumes of FDI and generate employment. The other major advantages are improved financial sector sophistication and improved GDP mix, as the proportion of tertiary sector increases.

Financial centres can be classified according to their importance and the areas they are catering to: as national centres catering to the local requirements of the nation state; regional centres, catering to a geographical region and as international centres, catering to financial service demands across the world.

1.3. Models of Development of Financial Centres

Financial Centres (FCs) have followed different models to get to where they are today. Some models of development have been less successful than others. However, the ability to move first has always been critical. London, Singapore and Hong Kong have become big financial centres by leveraging their position as a key trade centres. However, a mixture of fair regulation, market reforms and incentives have helped consolidate the position of these centres. Another key driver for financial centres has been the requirement to serve a large and sophisticated market. New York is the prime example of such a centre. Both demand for capital and sophistication of markets are key for success. Tokyo suffered because of lack of sophistication as a market. Japan is not open enough as a society. Language and lack of transparency alongwith high regulation and low responsiveness were also barriers to its growth. Frankfurt suffered from inadequate demand for capital and lack of flexibility and responsiveness. Another route for development of a financial centre is through the offshore centre route. However, such centres are increasingly coming under the scrutiny of international law enforcement agencies.

1.4. The future of financial centres

One school of thought favours the consolidation of high value added services as a corollary of the theory of clusters. The clusters would be supported by networking and technology services. Clustering of services not only leads to development of markets and building of core competence but also leads to improved competition between various intermediaries. This phenomenon has also been seen in other sectors like Silicon Valley, Bangalore for software and Surat for diamonds.

However, it is clear there will be a dramatic rise in overall global financial activity. Successful centres will have to position themselves to gain more than a proportional share of the incremental activity. Presently, many commoditised financial activities are being transferred to lower cost locations, where the requisite skills are available in plenty just as labour intensive manufacturing moved in search of lower costs. By gaining competence in these activities, these cities may soon be considered as a location of control of regional operations with a far higher level of valued added work content.

However, with increasing deregulation of more markets and technology-enabled solutions, there will be a large volume of global financial business being generated. It is important for a centre like Mumbai to accelerate to a level of sophistication required to retain a more than proportionate share of the resulting high value financial business transactions.

1.5. Some Key Financial Centres in Asia

Asia has seen a large number of serious contenders aspiring to become the next most important financial centre in the region after Tokyo and Hong Kong. While Tokyo and Singapore are the undisputed financial centre in the area, the Asian crisis, and the takeover of Hong Kong by China has provided an opportunity for other aspiring centres such as Shanghai. Bangkok, Jakarta and Taipei also have been planning to play a larger role in financial activity in the region, while Colombo's plans have been thwarted on account of the law and order situation in the country. Malaysia has positioned Labuan as an Offshore Banking Centre with a separate Offshore Banking Act.

The present volume of financial activity is a clear indication of the likely consolidation in the future, under normal circumstances. However, there could be structural changes such as financial crises, superlative growth prospects, rapid liberalisation, etc. which could attract increasing global attention towards new centres, given the right environment. The key characteristics of some of these centres have been discussed below:

Hong Kong

Hong Kong placed no impediments to the free flow of financial resources. Non-interventionist economic policies, complete freedom of foreign capital movement through the country and a transparent, non-ideological, predictable, accountable and well-understood regulatory and legal environment have greatly facilitated Hong Kong's growing role as a regional and international financial centre. Hong Kong still remains an important Asian base for International corporate and investment banking and forex markets. However its position as the number one regional financial centre of Asia (excluding Japan) is being seriously threatened by Singapore. The Hong Kong Government has reiterated its commitment to the international investment community to provide a sound economy and a base for investment. This commitment to ensure financial soundness and stability could not be better demonstrated than by HKMA's intervention in the stock and futures markets in August 1998 by spending USD 15.3 billion to prevent speculators from manipulating the financial market. Moreover, Hong Kong provides a highly efficient, productive, responsive working and living environment.

Singapore

Singapore is emerging as a key centre for regional fund management and corporate finance teams in Asia. Singapore secured the top spot in the 1999 World Economic Forum (WEF) ranking of economic competitiveness, ahead of the United States (2nd) and Hong Kong (3rd). Singapore's model of development has been one of managed consolidation. This has been aided by political stability, which has enabled the government to adopt economic and social policies in the best interests of the island nation. Singapore has liberalised its markets in a gradual manner. The banking sector was effectively protected from competition for a long period and has given a mandate to modernise. In the process Singapore created a sound and well-capitalised domestic financial system, which is the very backbone of a regional financial centre.

Lujiazui (Pudong region in Shanghai)

While Lujiazui is at present a relatively lower cost location among existing financial centres in Asia, it will take time to gain significant business volumes. The Chinese authorities intend to follow a clear and focussed action plan to convert the centre into an important regional financial centre and later to an important international centre. With the entire Chinese economy to ride on, Lujiazui has a right backbone for the planned transition. Initially, Lujiazui hopes to make significant gains, partly at the expense of Hong Kong. However, if Chinese authorities persist with experiments with economic liberalisation in Lujiazui, it could well become another attractive trade and financial services base in Asia.

1.6. Advantage India

India has the key ingredients for development of a regional financial centre with a reasonably big and fast growing economy. Moreover, the expected knowledge fuelled growth in the Indian economy will provide the right platform for development of the financial centre. The development of a financial centre in India is also aided by the advantageous geographical location between other financial centres in the East and the West, and availability of skilled English speaking workforce. India's stable economic infrastructure and a strong and stable politico-legal system also strengthens India's case for a future financial centre to be developed. Increasingly, India is also becoming the hub of regional operations for many multinational companies. However, India also faces competition from other destinations like Shanghai. in order to become a more attractive destination for foreign investment, India would need to increase the pace of reforms in the financial sector, along with the legal labour and social sector, especially the capital markets and reduce the levels of controls on the financial system.

1.7. Why Mumbai

The city of Mumbai is best suited to be a financial centre in India. The key advantages of Mumbai vis-a-vis other centres in India are:

1. Clustering of financial institutions and market participants in Mumbai
2. Mumbai is the centre of capital markets in India - both equity and debt
3. Mumbai has the highest concentration of financial intermediaries and allied service providers
4. Mumbai has the highest concentration of skilled workforce in India and has a professional and international work culture.
5. Mumbai is the centre of trade and commerce

Mumbai is well positioned to pursue the regional financial centre strategy. However, to make this a reality, steps need to be undertaken to:

1. Identify a strategic position for Mumbai as a regional financial centre
2. Identify the high profile financial service activities to be attracted to Mumbai to capitalise on the growth
3. Ensure coordinated working with local bodies and regulatory authorities to meet common objectives which are
   - ✓ Enable competitiveness in cost of establishment in Mumbai
   - ✓ Undertake critical urban infrastructure and transport capacity creation / upgradation on a war footing
   - ✓ Develop financial markets for greater sophistication

1.8. Positioning Mumbai

The following factors have contributed to the creation of successful financial centres in the past.

a) Consolidation of a first mover advantage as a key trading centre
b) Domestic demand for high quality financial services arising from the hinterland or from being a critical centre for trade and industry
c) The offshore / "tax haven" model
d) Cost effectiveness as a financial services location

While Mumbai clearly has had a lead within India, a larger role as a financial centre in the Asian region is a more difficult proposition. The real sector in India is witnessing growth in certain areas. This includes the ***IT/Media/Entertainment/Telecom Sector*** and the ***Infrastructure Sector***. While the former has been identified as an engine for growth, the latter cannot afford to be left behind, given the tremendous demand for infrastructure services. Growth in these sectors will draw upon sophisticated financial services and large volumes of funds both from India and abroad.

A Financial Centre at Mumbai should aim at:

a) Attracting financial business associated with these sectors in India
b) Attracting providers of required financial services
c) Exporting skills over the long term to other centres

Thus, the role of Mumbai, as a regional financial centre will arise out of the requirements of the new economy sectors of IT/Entertainment/Media and Telecom, the infrastructure sector and the privatisation requirements of the large public sector of India.

1.9. Attract Key Financial Services Providers to RFC Mumbai

The financing of new economy sectors and Infrastructure financing provide an opportunity for Indian financial services companies to participate in. As discussed before Mumbai should concentrate on building a strong base in 4 to 5 key financial services segments which will aid these sectors. Services like Private Equity/Venture Capital. Corporate Finance, Investment Banking, Asset Management, Broking, Insurance and Offshore Banking would be key for the development of a financial centre in Mumbai. Mumbai can also aim to provide innovative structures for domestic and international trade finance in conjunction with the SEZs.

Private Equity/ Venture Capital providers

The Venture Capital pool in Hong Kong is 5.5% of the country's GDP, with similar figures in Singapore and South Korea. In India, the pool size is far lower at 0.5% of GDP. However this funding source has certain advantages such as

- Longer term foreign investment than normal FII investments
- More management oriented approach to investment
- High projected investment growth rates in India

Financial Service Institutions

This sector provides an attractive opportunity for Mumbai to capitalise on. The different regulators have to operate in close coordination while evolving regulatory guidelines and framework, to ensure that common objectives, such as shifting of a larger base of venture capitalists, to India are met.

Hub activities of international financial institutions are mostly based in Singapore or Hong Kong. Shifting these operations to India will be difficult given that the important positions are occupied by locals. Moreover the top management enjoys an excellent quality lifestyle at these locations. However Mumbai should focus on attracting the **hub**

activities of Indian and regional financial services institutions planning to establish operations in Asia.

Insurance

Mumbai has an advantage in attracting insurance sector as most of the potential JV participants are already established in the city. Mumbai and Maharashtra also form an attractive market to target in the initial period of operations.

1.10. Develop Domestic Markets

The Stock Exchanges

The Indian equity market at present has an estimated market capitalization of $ 230 billion, which is comparable to most of the other markets in the region with the exception of Japan. The liquidity and depth in the markets have shown significant improvement over the last 2 years especially after the securities scam in 1993-94. However among the main players, foreign institutional investors, brokers and asset management companies the market is still controlled to a large extent by the first two entities.

Strong financial markets are the pride of the financial centres of international repute. These markets have become significantly developed on account of catering to a wide base demand from the domestic environment. Today markets such as NASDAQ and New York's NYSE are listing both international debt and equity offerings. Europe's equity markets are also undergoing a phase of consolidation.

An active securities and derivative market is critical for a sophisticated financial centre. Indian markets are evolving at a gradual pace aided by gradual financial reform. However, with increasing globalisation, it is important for regulators to liberalise these markets fast, so that they may evolve as dominant markets in the region in terms of depth and sophistication.

Money Markets

This money market includes call money, notice money, certificates of deposits and other short-term monies. This market is presently unorganised in nature and most trading activity is conducted between banks on a daily basis. Recent improvements include the development of **MIBOR** (*Mumbai Interbank Offer Rate*), a benchmark rate for 3 month domestic interbank borrowing rates but little placement occurs on the basis of the benchmark.

It is important that a screen based systems of quotes for the funds market is developed and strengthened to bring in transparency into the term money market. The Vaghul Committee as well as the Sodhani Committee, 1995 had recommended various measure on developing a term money market in India. The real impetus for money market development will come only after a mechanism to set accepted benchmark rates is introduced.

Debt Markets

The Indian debt market comprises of government paper (Gilt) and corporate bonds. A developed debt market provides access to debt of the required duration at reasonable and market determined costs. It also provides investors a fair degree of liquidity to enter and exit their investments at reasonable cost.

Though the Gilt market is mainly a telephone market, there has been growing liquidity in this market over the last few years encouraged by the gradual interest rate deregulation and the RBI's mark-to-market investment accounting requirement for banks. An increasing volume of the market has been moving to the NSE online system. Corporate debt instruments with over 18 months of initial maturity are mandated to be listed on the NSE online system.

It is important for the markets to establish a transparent and credible price discovery process in the primary market and a vibrant, liquid and broadbased secondary market. At the same time it is important to constantly enable more sophisticated instruments and transactions on the market while at the same ensuring a smooth, well functioning and efficient dealing and settlement system. The absence of short selling of securities on the debt markets is one such measure that impedes effective operations of operators.

With the opening of the insurance, to private sector participants there will be greater number of players in the debt markets. Secondly management of EPFs (Employee Provident Fund) by professional AMCs will also bring a wider number of securities under active management. Other reforms such as permitting new private and public provident and pension funds and relaxing investment guidelines will have positive impact on the debt market evolution.

International Banking

The ability to conduct international business is an important component of any aspiring financial centre. Financial centres in Asia where exchange controls still prevail usually allow offshore banks to operate in a controlled manner. The Sodhani committee (Expert Group on Foreign Exchange Markets in India 1995) had recommended the establishment of an international banking centre as a phased plan to achieving integration of India's market with the world markets, i.e. the stage when India allow convertibility of the rupee on the capital account.

Minimum necessary regulations

A separate **International Banking Act** will have to be enacted, under which International Banking Units (IBUs) will be regulated. While liabilities of IBUs will be exempt from local reserve requirements (to allow pricing in line with international levels) RBI can specify minimum liquid assets. Concessions will have to be negotiated with the CBDT to ensure that Income tax rates are comparable to that of other leading destinations across the world. Withholding tax exemptions on interest income of non-resident deposits will definitely enable business volumes to grow. However nominal tax should be effected. Also the units should be exempt from stamp duty for transfer of loans and other activities. Setting up an offshore centre is an important step in the smooth transition to capital account convertibility.

1.11. Evolution of RFC Mumbai

Given Mumbai's current advantages, its ability to attract capital and play a large role in the regional financial business, depends on three main factors:

- The relative state of financial liberalisation in India
- Total quality adjusted cost of establishment in Mumbai
- Provision of good quality public education

The State Government should focus on creating the right infrastructure amenities and pushing forward reforms to reduce costs of establishment. The state government should also work to improve public education, so as to maintain a good supply of skilled workforce for the financial centre. While the State Government may work with the Central Government and Regulatory bodies on urging financial reforms, this may take far longer in reality.

1.12. Proposed Interim Office Location Plan

Besides the issue of reforms in the financial sector, the key area to be addressed is the infrastructure to support the increased office space, housing, transport and telecommunication requirements of the emerging financial centre. As mentioned earlier, the key issue of reducing the quality adjusted costs to lower than the competition would need a comprehensive overhaul of the existing social and physical infrastructure and can be only achieved over a period time. However, given the peculiar problems of Mumbai, regarding availability of space and efficient transportation, especially in South Mumbai commercial hub, a three-node approach has been proposed based on the existing and soon to be implemented transport and office infrastructure. The system envisages three centres of activity:

- Corporate offices and existing financial sector participants in South Mumbai

- ❑ The new international financial centre with mid-office focus at the Bandra Kurla Complex
- ❑ Back office and Financial support centre at Andheri and Belapur CBD

The centres would need to be connected through high-speed telecom links for fast and voluminous data transfer and connectivity. A fast and economical transport link for providing access to the financial centres and transport between these centres would need to be developed.

1.13. Conclusion

It is established that an International finance centre not only helps in developing a good reputation, but also leads to improved employment opportunities, increased foreign investment and the development of the economy. India with its emerging economy status and impending knowledge driven growth and infrastructure requirements is a suitable place for development of a financial centre and is ideally placed to reap its benefits. Within India, Mumbai, being the national financial capital has a significant first mover advantage, which is very important for development of a financial centre. Mumbai, also enjoys the advantage of concentration of financial sector participants, being the centre of capital markets and the largest trade and commerce centre, besides having the best skill pool in India. Thus, Mumbai is ideally placed to pursue the regional financial centre strategy.

However, to make this a reality certain steps need to be undertaken to identify a strategic position for Mumbai, identify the activities to be attracted to Mumbai, ensure reduction in quality adjusted costs and ensure the development and strengthening of the markets. This would involve targeted regulatory changes and financial sector reforms and improvement in transport and urban infrastructure in Mumbai to reduce the quality adjusted cost of operations.

1.14. Action Plan

Government of Maharashtra

- Key Initiatives to prevent dispersion to other centres
  - Provide cost effective infrastructure
    - ➢ Improve land & housing legislation - ULCRA, Rent Act
    - ➢ Increase FSI in Nariman Point
    - ➢ Free mill lands
    - ➢ Improve transportation links between the proposed hubs
- Rationalise stamp duty

- Lobby with Central Government to move pension and insurance regulators to Mumbai

Ministry of Finance and Reserve Bank of India

- Rationalise legislation relating to Banking services
- Shifting Insurance and Pension regulators to Mumbai

Securities Exchange Board of India

- Rationalise capital market legislations

MTNL/DOT/VSNL

- Improve telecom Infrastructure
- Setting of a dedicated broad band network within Mumbai for financial services

MUMBAI AS A REGIONAL FINANCIAL CENTRE

1. Background to the Study

1.1. Bombay First

Bombay First – a initiative for economic and social development of Mumbai

Bombay First is an initiative of the corporate houses associated with the Bombay Chamber of Commerce and Industry. It was set up with the vision to help improve the economic and the social infrastructure of the city and to improve the quality of life of its citizens. Bombay First functions through 6 committees looking into different areas namely – Financial Services, Telecommunications, Land Use and Housing, Transport, Solid Waste Management and Research.

Bombay First had invited CRISIL to undertake a brief study and presenting the road map for the development of Mumbai as an international financial centre.

1.2. Objective, Scope and Deliverables

Study development of other financial centres

Objective

To prepare a roadmap for developing Mumbai as an International Financial Centre.

Develop a Roadmap for Mumbai.

Scope and Deliverables

The deliverables would include a report covering the following:

- evolution of financial centres and the forces that contribute to the success or decline
- positioning of other regional financial centres such as Hong Kong, Tokyo, etc. and a comparison of regulatory environments
- unique selling proposition and niche areas for Mumbai
- types of financial services to be provided
- investors, depositors, regulators and other participants
- identification of hard and soft infrastructure requirements

Regional Financial Centres like Singapore, Hong Kong, Shanghai discussed

Road map for development

1.3. Approach & Methodology

Survey of Regional Financial Centres

The objective of this module is to present an overview of the regional financial centres such as Tokyo, Hong Kong, Singapore, Taipei etc. This is with a view to developing an appropriate focus for an international financial centre in Mumbai.

Most of the financial centres are developed with a focus; e.g. Shanghai is being positioned as an alternate centre for channeling foreign funds into China. Tokyo provides a gateway to the Japanese financial market and integrates the Japanese economy with the international economy. Similarly financial centres in the West such as London, Luxembourg and Switzerland have a prominent presence, with their own special focus and positioning.

Some of the roles being explored for Mumbai include that of a Gateway for FDI into India, a domestic centre for venture capital and that a centre for offshore lending and borrowing.

Development of a Road Map

This module of the assignment involved extensive research. Data from various agencies involved in the development of financial centres worldwide, such as Hong Kong Monetary Authority, Economic Development Board of Singapore, Monetary Authority of Singapore, Finanzplatz Deutschland etc have been compiled and analysed.

This module traces the following, for financial centres in direct competition with Mumbai

- Growth into centres of prominence
- Focus areas, strengths and weaknesses and their USPs
- Key financial services and regulatory environments
- Participants and interface with regulators
- Hard and soft infrastructure

The objective of this module is to present a road map for the transformation of Mumbai as a regional financial centre before gradually developing into a financial centre of international importance.

This module draws heavily upon meetings with experienced professionals in the financial services industry, allied service providers, regulators and policy makers. Meetings with different financial services providers and regulators are currently underway. Past and current studies, both in areas of financial reform, infrastructure development and strategy reports, which have been undertaken in the above areas are being accessed in order to develop the integrated roadmap for Mumbai.

The following aspects have been covered under this module:

Financial Services

- key financial services to be provided
- summary of regulatory and legal environment required for these financial services
- summary of steps required for the development of the domestic capital markets
- measures to attract target participants

Infrastructure

- Critical infrastructure requirements to address gaps
- Other "quality of life" factors to be addressed
- Steps needed to be undertaken by State government / Central government

2. Introduction

An international financial centre provides specialised financial services on a global scale. The international financial centre status brings about international prominence, remarkable employment opportunities and a transformation to a high value service based economy. As a result the networks of financial centres is expanding with many contenders vying for a large share of global financial services pie.

Few cities can aspire to become a financial centre of the magnitude of London or a New York. However some locations are blessed with certain advantages that put them in a superior position to evolve into a financial centre. Mumbai is one such centre having already established its position as the financial capital of India.

Financial Centres attract high volumes of FDI and generate employment

It is not without reason that every national financial capital in the Asian region has attempted to attract top international corporate headquarters to their main cities. National prestige is only one of the factors, as other benefits are clearly more dominant. Countries such as Japan, Thailand, Hong Kong and Singapore have all been affected by the Asian crisis to varying extent. At this point in time, these countries are exploring means through which they can strengthen and diversify their economies, further reform different sectors and attract capital. Moreover the devaluation of currencies in the region has made them attractive locations for foreign investments. These countries in turn have opportunities to gain on fronts, such as increased employment and increased Foreign Direct Investment.

It is in this context that Mumbai will also have to carefully decide a plan of action to become a dominant centre in the region. Mumbai's advantages are that, it has a large population of highly skilled English speaking workers and a reputation for attracting the best managerial talent in India. It is important that Mumbai gears itself to retain a large volume of the potentially high value financial activity that India has to offer and also a significant portion of activity from the Asian region.

Key advantages of financial centres

Mumbai has to capitalise on its advantages and develop into a regional financial centre or be left out in the race. The city has to adopt the model role to support this transition and thereafter position itself into a centre of international importance. The transition brings with it many advantages.

Employment generation

Financial services is a boom industry, which has the potential to create large employment directly or indirectly. Being highly technology driven, finance has a potential to create employment in associated sectors like software and telecommunications. Additionally, having an international financial centre enables sectors such as tourism to get a boost, by giving international exposure to other parts of the country.

Improved financial Sector sophistication

A country needs an innovative and competent financial centre in order to provide a) the cheapest sources of capital for its industries and b) the best risk management practices, so that a nation's real sector continues to remain competitive. An international financial centre will impart valuable international experience to local banks / financial institutions on account of its proximity to world class competence. On the other hand, it will increase depth and scope of financial services available to importers, exporters, industry and investors.

Improve GDP mix by moving up the activity value chain

Most financial centres have a high component of service activities contributing to their GDP. Many of the service sector activities can be highly value added, requiring more intellectual capital than core assets, and are essentially non-polluting. Exports of value added services can bring in significant foreign exchange, in much the same manner that Indian software industry is contributing to the GDP and the balance of trade.

The Bombay First Initiative.

This report is structured in three parts. The first section deals with trends currently visible in the international landscape concerning financial centres and the implications of these developments for Mumbai.
The second part of the report compares the growth of Singapore and Hong Kong as major financial centres in the Asian region as well as the ambitions of other national capitals in the region.

The third part of the report discusses the model role for Mumbai, and suggests an action plan in order support this transition into a centre of international importance.

3. Models of Development of Financial Centres

Financial Centres (FCs) have followed different models to get to where they are today. Some models of development have been less successful than others. The ability to move first has also been critical. This chapter explores some of the common models of development of financial centres.

3.1. Traditional Reasons for Emergence of FCs

Key Trade Centre

London, Singapore and Hong Kong have emerged as FCs primarily because of the trade activity that took place around these centres. Centred on trade, institutions providing various financial services such as trade financing, merchant banking and insurance, developed leading to the development of the centre. The location of the centre was also critical to the success of this model. In the case of Hong Kong over 80% of the exports from China are still being re-exported through Hong Kong. These trade centres have evolved into financial centres by encouraging financial services to base operations there. A mix of fair regulation, market reforms and incentives have helped consolidate the positions of these centres. These centres have clearly not had the need to position themselves as tax havens to attract capital. Notwithstanding this, present rates of taxation are lower than that of most other centres.

Centre serving large & sophisticated markets

New York is a centre that rose into prominence on account of a large and sophisticated domestic market for capital, driven by the industrial revolution and an unparalleled entrepreneurial spirit. New York was just one of the many centres in the USA, which at one point in the late 1800s, had over 100 stock exchanges. New York's rise to prominence came with the introduction of the tickertape in the early 1900's by which price information on stocks listed on the NYSE could be seen by the trading members of the NYSE.

New York City has become a world financial centre, attracting the largest national and international corporations. It is the home to three stock exchanges and 47 Fortune 500 companies, more, in fact, than any other city in the USA. Revenues from banking, insurance and investment account for the greatest portion of the city's economy and are measured in USD trillions. Despite controls on financial markets that lasted a good part of the 20th century, New York's financial innovation has been one of the most critical reasons for its position of dominance.

Supporting the financial sector is New York's sophisticated telecommunications system. Approximately one third of all overseas business calls in the U.S. are placed from the New York area and as much as $1 trillion in financial transactions flow through the city's vast series of telecommunications networks each day.

If either factor i.e. demand for capital and sophistication of market is missing, it is less likely to be successful. Tokyo is a case in point where the demand for financial services has been very high but where market sophistication failed to occur on account of a highly regulated financial system. Frankfurt on the other hand, represented a case where the markets were fairly sophisticated, but lacked adequate domestic or international demand. Needless to say both financial centres have only been reasonably successful. However, with the introduction of the Euro, Frankfurt's fortunes might change.

Offshore based model

The offshore financial centre model has been pursued by centres attempting to attract offshore capital irrespective of source, by setting a low taxation regime and strict banking secrecy laws. Capital has come to these centres seeking protection from possible expropriation more than the absence of taxation. These centres also take advantage of double taxation treaties with specific countries and some of them even apply strict banking secrecy laws. Many such centres, known as "brass plate" centres, have come up while many more have disappeared from prominence. This model relies on very light regulatory environment and low taxation with the absence of exchange controls of any nature.

Some of the centres that have relied on this model have increasingly come under very tight scrutiny of international law enforcement agencies as the money routed through these centres have been through illegal means (drug running, arms smuggling etc.). There is mounting pressure on governments at these centres to provide access to details on large numbered accounts.

The European Union and the Organisation of Economic Cooperation and Development have commenced their moves against "harmful tax competition" from these centres and are creating an offshore centres blacklist, which is expected to come out by June 2000.

These centres are also subject to high-risk banking as until the critical mass is reached, these centres may face large withdrawals of funds, which could impact liquidity.

3.2. Conclusion

Most financial centres have risen into prominence because of the development of skills and services to support the financial requirements of a strong and growing ***real sector***.

First movers have advantages

While ***first movers*** have retained significant advantages in their quest for international status, external factors have dictated that constant ***evolution*** has also been necessary to sustain the same.

In Asia, increasing deregulation and costs have a strong bearing on capital flows and established centres cannot take their positions for granted. Technology also contributes to changing business rules. Each possible contender for the regional financial centre will therefore have to carefully plan strategies that will result in gaining a large volume of the regional financial business. Switching costs will thereafter ensure that the first mover advantage remains for a reasonable period of time.
Many other centres have attempted the rise to fortune, by projecting a tax haven status, but this model has high risks of regulation, because of the changing international perspective on activities conducted, that may not make it attractive.

4. The future of financial centres

Dr. Saskia Sassen, Professor of Sociology, University of Chicago, an authority on global cities, has conjectured that the two main factors stand out in turning an ordinary city into a global financial centre. The first is national consolidation while the second is market liberalization. An example of the first include New York where the concentration of investment banks and dominance of the domestic stock exchanges have left its other US rivals far behind. Similarly Sydney, Toronto, Mumbai, Paris have assumed national dominance.

The number of cities joining the global financial club is growing sharply as countries are deregulating their economies. Forces such as changing technology, devaluation of currencies and deregulation of financial markets definitely have an impact on the future of financial centres. These forces open up channels for cross border investments into the countries through these cities, which then become gateways.

Despite the rise of new centres, there are two different schools of thought on whether financial activity will essentially consolidate or disperse across many centres. However, it is clear there will be a dramatic rise in overall global financial activity. Successful centres will have to position themselves to gain more than a proportional share of the incremental activity.

4.1. The Consolidation Theory

Consolidation of high value financial services at established IFCs supported by ...

With changing technology and increasing globalization there are reasons to argue whether financial services will get consolidated at existing financial centres or will get dispersed.

The consolidation theory argues that most high value financial services activities will get concentrated at a few key international financial centres. These include activities such as strategic consulting, management of global portfolios, allocation decisions, patching together cross border M&A deals etc. Many markets need a base for operations and executive decision-making given complications of working in a decentralised business.

Networking and technology advances

One of the supporting arguments for the consolidation theory is that of networking of different centres. Since networking reduces barriers to information flows, banks can afford to consolidate different treasury departments across the globe at a single location. Today close to 60% of London's Eurodollar market is handled by Reuters 2000 and EBS (Electronic Brokerage systems). Information required for trading decisions are released to the market almost instantly via these systems. Agency trading (deals on behalf of agents) can be clearly conducted from a single location), reducing the costs of locating in multiple cities. A case example is BHF Bank, Frankfurt which has concentrated its 24 hour trading operations in Frankfurt and services all global requirements from there in 3 shifts.

However in the case of equities, trading the same rationale for consolidation may not apply. There is a lot more than factual data that goes into markets and they generally tend to exhibit weak forms of efficiency. Local presence is considered necessary for success.

Management control requires centralisation of financial services

Secondly, internationally banks are focusing on centralizing the riskiest parts of a business, such as market and operational risk management at a single location. Instances such as the collapse of Barings Bank have made bank managements more cautious. This can be done best, if main activities such as trading, global accounting, settlement etc. are concentrated at a single location.

Development of markets

Centralization of lending activities can be undertaken from remote locations if securitisation develops in different markets. As debt markets around the world evolve and barriers to capital flows disappear, securitisation reduces the need for large international banks to have more than a marketing presence in various markets.

Need for building core competence

Clustering of financial services activities, clients and providers of capital is an effective way of improving competitiveness and encouraging innovation of the financial centre. A case example is Silicon Valley in the USA for software development. The clusters of competence attract new service providers to themselves given a conducive environment.

4.2. The Dispersion Theory

Capital and skills, two critical components that go towards making a successful financial centre are easily transferable given favourable regulation and opportunity. This supports the argument that it is indeed possible to attract financial services to a particular centre through the right combination of factors.

Dispersion of financial centre activities supported by ....

Of critical importance to capital markets is the ability to operate in an environment, which is efficient, predictable and low cost. For example, many international financial centres have already learnt that the imposition of a withholding tax, which is not matched by other financial centres, serves only to encourage the industry to move elsewhere. The recent global trend has been to announce the removal of withholding on non-resident bonds (e.g. Japan, Australia and Greece).

The development of the Eurodollar market centred around London illustrates the classic example of how London capitalised on opportunities provided by dollars generated outside USA. Following the introduction by the US of the "equalisation" (withholding) tax on income from externally owned dollar deposits, UK created certain conditions that drove the eurodollar market away from New York to London. This led to the recovery of London as a major international financial capital.

Cost of operations at large centres reducing profitability

It has been observed that financial services activities are getting increasingly dispersed. One of the main drivers is **cost** of operations. In an era of shrinking margins on account of high competition, companies have relocated headquarters from more expensive locations to less expensive locations. Often the shift has also occurred within the same city. Big financial centres are expensive places to conduct an increasingly global business from and technology has supported such shifts.

Proximity to customer for a wide range of business.

Proximity to the customer is critical for a wide range of financial transactions. Local practices vary across locations and it becomes important to retain a domestic presence in each of these centres. Relationship management teams, local product teams and other activities that require regular client interaction have to be based in the given location.

Light regulatory environment attracts capital

Regulation is constantly changing from centre to centre. Capital flows are largely determined by **light regulation.** A location that holds promise of tremendous opportunities may only become attractive after gradual deregulation.

4.3. Conclusion

Shifting of commoditised financial activities to low cost locations

Presently, many commoditised financial activities are being transferred to lower cost locations, where the requisite skills are available in plenty, just as labour intensive manufacturing moved in search of lower costs. By gaining competence in these activities, these cities may soon be considered by corporates as a location for control of regional operations with a far higher level of valued added work content.

Concentration of high value activities

Traditionally high value added financial activity are most likely to remain concentrated at some venues aided by rapid technology changes and costs. There are opportunities to attract newly developing financial businesses to emerging centres provided the right environment is created.

Overall increase in global financial activity – opportunity for Mumbai

There will, however, be a large volume of global financial business with deregulation of more markets and technology enabled solutions. It is important for a centre like Mumbai to accelerate to a level of sophistication required to retain a more than proportionate share of the resulting high value financial business transactions.

The transition will have to be accompanied by a clear focus on financial reforms to attract further financial services and incentives to attract world class players and development of financial markets. Strategies to become a competitive centre in terms of total costs of establishment are also crucial.

In few circumstances have financial centres been able to sustain their advantages irrespective of environmental changes. Wherever it has been possible, successful financial centres have constantly evolved in order to retain their positions of dominance. The following section traces the evolution of dominant financial centres in the Asian region, in order to benchmark Mumbai against these centres.

5. Financial Centres : Mumbai's Competitors

Asia has seen a large number of serious contenders aspiring to become the next most important financial centre in the region after Tokyo and Hong Kong. While Tokyo is the undisputed financial centre in the area, the Asian crisis, and the takeover of Hong Kong by China has provided an opportunity to the other aspiring centres such as Singapore to gain. Bangkok, Jakarta and Taipei also have been attempting to play a larger role in financial activity in the region, while Colombo's plans have been thwarted on account of the law and order position in the country. Malaysia has positioned Labuan as a Offshore Banking Centre with a separate Offshore Banking Act.

This chapter compares key aspects of financial systems in different markets with specific focus on a) the model of development as a financial centre b) financial systems sophistication and weaknesses of different centres.

The present volume of financial activity is a clear indication of likely consolidation in the future, under normal circumstances. However there could be structural changes such as financial crises, superlative growth prospects, rapid liberalisation etc. which could attract increasing global attention towards new centres, given the right environment.

Category	Singapore	Hong Kong
Economic Freedom Index (Rank)	2	1
GDP per capita (Rank : PPP estimates)	4	8
Cross border banking (% of world share)	5%	5%
Foreign exchange market (% of world share)	7%	4%
Exchange Traded Derivatives Turnover (% of world share)	1%	0%

Source : BIS, Spotlight London, Heritage Foundation

5.1. Hong Kong

Hong Kong placed no impediments to the free flow of financial resources. Non-interventionist economic policies, complete freedom of capital movement and a well-understood regulatory and legal environment have greatly facilitated Hong Kong's growing role as a regional and international financial centre.

Banking System

- The Hong Kong Monetary Authority (HKMA) functions as the de facto central bank. The HKMA is responsible for maintaining the stability of the banking system and managing the Exchange Fund backing Hong Kong's currency - linked to the U.S. dollar at Hong Kong $7.8 = US$1.

- By the end of 1998, Hong Kong had 172 licensed banks (141 were incorporated overseas), 60 restricted licensed banks (25 were incorporated overseas), 101 deposit-taking institutions (two were incorporated overseas), and 141 representative offices (all were set up by foreign banks).

- Credit is allocated strictly on market terms and is available to foreign investors on a non-discriminatory basis. The private sector has access to the full spectrum of credit instruments as provided by Hong Kong's banking and financial system.

- HKMA, with the assistance of the banking sector, has upgraded Hong Kong's financial market infrastructure. The interbank payment system based on Real Time Gross Settlement principles was installed in December 1996. The new system helps minimize risks in the payment system and brings Hong Kong in line with international standards.

Insurance

- Insurance companies are authorized by the Insurance Authority to transact business in Hong Kong, which has the highest number of authorized insurance companies in Asia. At end 1998, there were 209 authorized companies: of which 104 were foreign companies from 27 countries. 6 out of the world's 10 top insurance companies (in terms of assets) have branch offices or subsidiaries in Hong Kong.

- In addition, premium income from insurance services in Hong Kong is the 5th highest in Asia (after Japan, South Korea, Taiwan and China) and the 24th highest in the world.

Stock and Futures Markets

- With a total market capitalization of US$ 341.3 billion and 680 listed firms at year-end 1998, the Stock Exchange of Hong Kong (SEHK) was ranked 2nd in Asia after Tokyo, and 11th in the world in terms of market capitalization. At the end of April 1999, the SEHK had grown to 684 firms with total market capitalization of US $ 433.5 billion.

- The Hong Kong Futures Exchange Ltd. provides a market for Hang Seng Index futures and options. At the end of 1998, futures contracts for seventeen local stocks were traded at the Exchange. ***The government is planning to merge and demutualise the stock and futures exchanges by early 2000.***

- There are no discriminatory legal constraints to foreign securities firms establishing in Hong Kong via branching, acquisition, or establishing subsidiaries. In practice, foreign firms typically establish in Hong Kong as subsidiaries. Rules governing operations are the same, irrespective of ownership. There are no restrictions on cross-border capital flows.

- The SEHK plays a significant role in raising capital for Chinese state-owned enterprises. Chinese state enterprises can raise equity (through the issuance of so-called "H" shares) in Hong Kong provided they meet Hong Kong regulatory and accounting requirements. These "H" shares are denominated in renminbi, but must be purchased in Hong Kong dollars. In 1998, a total of 41 Chinese enterprises had "H" share listings on the SEHK, with market capitalization of US$4.3 billion.

Debt Market

- Hong Kong dollar debt (public and private) has increased gradually, from US$3.46 billion at the end of 1989 to US$50 billion by the end of 1998. Since 1990, Hong Kong has made a concerted effort to develop a local debt market with the launching of the Exchange Fund bills and notes program. Maturities now extend to 10 years. Being a major regional centre, regional infrastructure financing requirements, continued high regional GDP growth rates, and increasing investor demand are projected to stimulate further development of the local debt market.

- In March 1997, the Hong Kong Mortgage Corporation (HKMC) was set up to promote the development of the secondary mortgage market in Hong Kong. The HKMC is 100 percent owned by the Government through the Exchange Fund. The HKMC purchases residential mortgage loans for its own retained portfolio, and then repackages mortgages into mortgage-backed securities for sale. In 1998, the HKMC has issued US$666.7 million worth of unsecured debt securities in the local debt market.

- Like most other Asian countries, mandatory provident fund for employees and worker was not compulsory till recently. Contributions are expected to channel U.S. $3 to 4 billion per year into various investment opportunities into the debt and equity markets. Schemes are expected to begin operations in early 2000. Portfolio investment decisions are left to the private sector without any restrictive investment guidelines on foreign investment, participation or control.

Openness to Foreign Investment

- Hong Kong has demonstrated an approach to foreign investment that is far more open than other countries in the region. Even Singapore, which has been. a serious competitor, has attracted foreign investment using a more cautious approach to opening up its economy.

- *Treatment of foreign investment:* Hong Kong welcomes foreign investment, without offering any special incentives or disincentives for foreign investors in the forms of tax breaks, limitations on the use or transfer of foreign currency, quotas, performance requirements or other similar regulations. Reporting requirements are straightforward. As a duty free port, the absence of tariff barriers have helped domestic and international firms in Hong Kong develop in a competitive manner.

- *Tax system:* Hong Kong's corporate taxation rates are reasonably low. This has attracted a larger number of players with Asian ambitions to Hong Kong. Foreign-owned and domestically owned firms are taxed at the same rate, 16% of profits. There is no capital gains tax, or withholding taxes on interest, dividends and royalties. Profits can be freely converted and remitted across Hong Kong's borders.

Weaknesses

- ***Cautious approach of foreign investors after reversion to China:*** Hong Kong has continued to enjoy substantial economic autonomy following its reversion to Chinese sovereignty on July 1, 1997. Chinese leaders repeatedly underscored China's intention to abide by the provisions of the Sino-British Joint Declaration and China's Basic Law for Hong Kong, which amplify the meaning of "one country, two systems" to include separate monetary systems, separate financial and regulatory systems and separate budgetary regimes. However foreign investors approach Hong Kong with more caution while planning an Asian investment base.

- ***China's own initiatives***: Hong Kong has received a lower level of importance in Asia after takeover by China primarily on account of China's own initiatives to promote the Shanghai – Pudong area as a major financial centre in the area. Hong Kong's trade economy depends on the re-export of Chinese goods which constitute over 80% of total exports of Hong Kong which will gradually move to China's own economy zones. This may dry up the accompanying financial service offerings (e.g. trade finance / insurance) with the emergence of new export zones on the mainland.

Conclusion

Hong Kong still remains an important base for Asian corporate banking and forex markets. However, its position as the number one regional financial centre of Asia. (excluding Japan) is being seriously threatened by Singapore. The Hong Kong Government has reiterated its commitment to the international investment community to provide a sound economy and a base for investment. This commitment to ensure financial soundness and stability could not be better demonstrated by the HKMA's intervention in the stock and futures markets in August 1998 by spending USD 15.3 million to prevent speculators from manipulating the financial market.

Singapore - The Hub of the Asian Dollar Market

The Asian dollar market, centred in Singapore, reflects the republic's success as a financial centre. The pool of resources in the market has expanded steadily since its inception. Total assets reached S$507 billion at the end of 1996. The steady expansion of the market has been stimulated by the government's tax concessions and exchange-control liberalisation measures. Financial institutions operating ACUs set up specifically to handle offshore business enjoy a concessionary 10% tax rate on all offshore income other than income from transactions with domestic banking units and residents. This incentive has been extended to include fund management of local stocks and shares, as well as MAS-approved fund managers without ACU licences.

5.2. Singapore

A diversified economy

Financial & business services (29% GDP) and manufacturing (22% GDP) are the key sectors of the Singapore economy. The other economic sectors are commerce, transport and communications (11.0%), construction (9.0% percent), and other services (12 percent).

Singapore is focussing on capitalising on the business services sector in order to support the recovery process after Asian crisis. This includes IT and Telecom services. There has been a strong public sector demand for information technology (IT) services (to intensify the use of IT in education). Secondly, Singapore has established of an electronic commerce infrastructure in the country and the rollout of Singapore ONE in 1998 (a countrywide high-speed fiber optic broadband network providing multimedia applications and internet services) will definitely boost the IT sector.

Focus on the knowledge based sector

Singapore has intensified efforts to strengthen its domestic economic fundamentals. These include:

- Restructuring its economy towards knowledge-based and high valued-added activities; pursuing workforce development strategies
- Undertaking financial sector reforms to become an international financial centre
- Developing new export markets

The budget has placed high priority on increased development spending on **education** and the **economic infrastructure**, aimed at preparing Singapore for the next growth wave after the Asian economic crisis.

Banking System

- The Monetary Authority of Singapore (MAS) regulates financial institutions in Singapore. The MAS performs the functions normally associated with a central bank, except for the issuance of currency, which the Board of Commissioners of Currency, Singapore (BCCS) is responsible for. Under statutory regulations, the BCCS must maintain external assets, such as gold and major world currencies, fully sufficient to back the domestic currency.

- Singapore's prominence as a financial centre is evident in the continuing increase in the number of international banks operating in its territory. At the end of March 1996, Singapore had 143 commercial banks, 79 merchant banks, 58 representative offices of banks and merchant banks, 22 finance companies and 10 international money brokers. Of the 143 commercial banks, 12 were local banks. Of the 131 foreign banks, 22 have full banking licenses, 14 have restricted banking licenses and 95 have offshore banking licenses.

- Amendments were made to the Banking Act to enhance the regulatory framework in Singapore in line with developments in the international financial markets and to strengthen the country's financial system. A bank's licence determines the scope of its operations. Banks are licensed under one of the following three categories:

Full license banks

- These banks may transact all types of banking business and, if they have an Asian Currency Unit (ACU) licence, may accept deposits and make loans in foreign currencies.

Restricted licence banks

- These banks engage in a full range of banking business, except that they are not permitted to
  - Accept time deposits of less than S$250,000
  - Operate saving accounts
  - Set up branch offices in the republic.

  Restricted licence banks typically hold ACU licences and are active in the wholesale corporate banking sector.

Offshore licence banks

> Offshore banks are prohibited from accepting Singapore-dollar deposits except from other banks and approved financial institutions. Banks with offshore licences engage primarily in Asian-dollar and foreign exchange transactions. They are also permitted to engage in Singapore dollar financing of local industries, but only to a limited extent. An offshore bank is allowed to extend up to a total of S$150 million in credit to residents of Singapore.

Securities and Commodities Exchanges

- The MAS also regulates the Stock Exchange of Singapore (SES), stockbroking companies and their representatives by administering the Securities Industry Act and Regulations. Singapore, unlike, India has the same regulator covering the banking, insurance and the securities sector. Singapore securities market systems were well in place by the mid-nineties. For example, scripless trading came into effect in 1993, and by June 1994 all companies in Singapore had converted to scripless trading.

The Main Stock Exchange

- **SES (Stock Exchange of Singapore)** : The SES is one of the largest stock exchanges in Asia, with market capitalisation of about USD 185 billion(June 1999). Trading volumes at SES (first half of 1999) touched 90.2 billion shares. The SES is one of the first exchanges in the world to have a fully computerised trading system. ***A direct communications link between the US National Association of Securities Dealers (NASD) and the SES enables Singapore investors to diversify their investment portfolios to include both US and European stocks.***

SES is typically for large companies with significant capital requirements. Broking companies are required to have

- adjusted net capital (ANC) of at least S$10 million
- aggregate indebtedness not exceeding 5 times the amount of the ANC
- a reserve fund

Investors may trade in equity securities of selected companies listed on the neighbouring Asian bourses. Stocks traded on the OTC market included those of Malaysian companies, Hong Kong, Australian, Taiwanese, Filipino and Indonesian companies.

The SESDAQ: This is a second securities market to allow enterprises to raise equity public funds without seeking a full listing on the Main Board of the SES. It is comparatively easier and cheaper to secure a listing on the SESDAQ.

Financial Futures Markets

- The Singapore International Monetary Exchange (SIMEX), Singapore's financial futures market, saw its trading volume rise to an all-time high of 3.24 million contracts in June 1999.
- SIMEX has a Mutual Offset System Agreement with the Chicago Mercantile Exchange (CME) to September 1999. Under this system, the first of its kind in the world, allows *a trading member to book a contract on one exchange and close it on the other.* This mechanism facilitates 24-hour trading of financial futures.

Insurance

- Singapore is a major insurance centre, home to a rich mix of leading insurers, reinsurers, captives and brokers. It aims to be the premier insurance hub in Asia by year 2003, overtaking Hong Kong.
- In 1998, total premiums of the insurance industry amounted to S$7.8 billion. Total gross premiums for the general insurance industry amounted to S$2.7 billion. Offshore business accounted for 40.7% of all general insurance premiums.
- Qualifying profits derived from insuring and reinsuring offshore general business risks benefit from a reduced taxation rate in Singapore. The reduced rate of tax (10%) also applies to profits earned from offshore life insurance business, and cross border banking business underwritten in Singapore.

- Singapore is aiming to further develop the direct general and reinsurance sectors of the insurance industry. Singapore aims to build up specialised areas like marine hull and the financial guarantee business, as well as attract more reinsurance players to Singapore.

Openness to Foreign Investment

- The Singapore government actively encourages free enterprise by providing tax and financial incentives to attract both local and foreign investment. These incentives ***are usually granted to industries that use high technology and skilled labour and require relatively few natural resources***. In granting these incentives, the government does not differentiate between foreign and local investment capital.

- Singapore has designated its Economic Development Board (EDB) to attract international service corporations to set up operations in Singapore. Singapore grants tax exemptions and holidays on a flexible basis, based on the type of activities that it wants to encourage in the island. These are typically high technology, engineering, computer-related and industrial-design products and other services. For example there are various tax incentives and holidays with a view to encourage
  - ✓ Venture capital investments
  - ✓ Investments in overseas enterprises
  - ✓ Remittance of foreign income / consultancy fees
  - ✓ Setting up regional operational HQs for MNCs
  - ✓ Profits from high value added financial services

Infrastructure : overcoming land shortage

- Singapore encourages multinationals to view Singapore, Johore (the southern-most state of Malaysia, which is linked to Singapore by a causeway) and Indonesia's island of Batam as a single investment region.

High technology and communications industries are attracted to plant sites in Singapore, and labour-intensive and intermediate plants may be built in either Johore or Batam. To promote the concept of reconfiguring operations, the authorities from the three countries have taken steps to enhance relations and co-operation. ***Singapore, Malaysia and Indonesia are gradually removing trade barriers and adapting internal policies to encourage three-region investments.***

Establishing IT & Telecom Infrastructure

Singapore's IT and telecommunications infrastructure, transportation services and utilities are highly developed. The phone-line penetration rate is on par with developed countries. One-third of Singaporeans have mobile phones and 70 percent own pagers. Over 40 percent of households own personal computers and almost one-fifth have internet access or subscriptions.

- To promote the growth of IT industries, the country has installed Singapore ONE, the nationwide high-speed fiber optic broadband network that provides multimedia applications and internet services to all homes, schools and offices. In a recent survey by the International Data Corp (IDC), Singapore was ranked the 4^{th} (after the USA, Sweden and Finland) most information-driven economy.

Other infrastructure

- The road system is well maintained, and road congestion is managed through the use of an electronic road pricing system (ERP) and a quota on the vehicle population. The public transportation system, which includes an efficient metro system, provides island-wide coverage at reasonable prices. Singapore's airport is also frequently surveyed as among the best in the world. The utilities network provides reliable services.

The government has also taken advantage of lower building costs during the lull period throughout the Asian economic crisis to intensify upgradation of physical economic infrastructure. These included

- Extending the metro line to the north-eastern part of Singapore and to the airport
- And engaging in reclamation works to increase the land stock of the city-state (total land area in Singapore is 650 square kilometers).

- Directing resources to Jurong Island, to house a vertically integrated petroleum and chemicals industry (a project estimated to cost over US$4.0 billion). Development of tourist attractions and mega-exhibition facilities.

Weaknesses

- ***Non performing loans from offshore banking business*** : Singapore was a base for the Asian Dollar market (the Asian equivalent to Europe's Euro Dollar Market). Offshore loans are provided to non-bank customers in Singapore's Asian Dollar Market, a thriving business for Singapore-based banks prior to the Asian crisis, which affected the business. As of March 1999, NPLs have risen to 24.3 percent and 8.0 percent of the regional and global loan portfolios, respectively, of Singapore banks. However, in terms of systemic risks this does not pose a major problem, as Singapore banks are generally well capitalised and well provisioned, more than BIS requirements.

Conclusion

Key regional financial centre

Managed consolidation and gradual opening

Singapore is emerging as a key centre for regional fund management and corporate finance teams in Asia. Singapore secured the top spot in the 1999 World Economic Forum (WEF) ranking of economic competitiveness, ahead of the United States (2nd) and Hong Kong (3rd). Singapore's model of development has been one of managed consolidation. This has been aided by political stability that has enabled the government to adopt economic and social policies in the best interests of the island nation. Singapore liberalised its markets in a gradual manner. The banking sector was effectively protected from competition for a long period and given a mandate to modernise. In the process Singapore created a sound and well capitlised domestic financial system, which is the backbone of a regional financial centre.[1]

[1] A list of financial sector reforms undertaken by Singapore Government to promote Singapore as a financial centre is given in the annexure.

5.3. Shanghai – Pudong Region

Lu-jia-zui : China' s financial centre

Shanghai is being promoted by China as a new financial centre. China nurtures ambitions of making Shanghai a regional centre in Asia. There are various other Special Economic Zones such as Shenzhen, Shantou, Zhuhai, Xiamen and Hainan, 14 coastal cities, dozens of development zones and designated inland cities which all promote investment with unique packages of tax incentives. **(The Pudong area in Shanghai is particularly noteworthy as a location for Chinese experiments in liberalization, which are then extended nationwide, if successful).**

A 28 square km. in the Shanghai-Pudong region, Lu-jia-zui, has been positioned as the national finance and trade zone. An advantage of this centre is that it's a product of a well-planned approach to a financial centre despite the fact that significant progress remains to be made.

Measures taken by the Chinese Government for the new centre

Lu-jia-zui not only enjoys a superior location, but also has the advantage of possessing specific functional objective. It is supported fully by the central government and Shanghai Municipality, it enjoys special finance and trade preferential policies apart from the preferential policies in other Special Economic Zones. Measures have been taken by the Chinese Government to promote the centre.

- Shifting Local banks into the area
- Allowing foreign-funded insurance companies to conduct insurance business within the zone after approval
- Incentives offered to foreign banks to relocate (in the form of preferential allotment of RMB business licenses for entire China when the regulations come into effect). 9 foreign banks, primarily Japanese have been allowed to conduct domestic (RMB) business in Lujiazui region which is not allowed in the rest of China. In 1996, foreign bank branches in the Shanghai Pudong area of were first allowed to engage in local currency business, though limited to providing

services to foreign-invested enterprises (FIEs)[2]. In 1998, China expanded the Pudong rules for local currency business to foreign banks in Shenzhen.

- Sino-foreign joint ventures dealing in foreign trade once approved can do business within the zone.
- Exchanges and trading centres of real estate, securities, metal, coal, cereal & oil, petroleum, etc., are being planned to be shifted to Lujiazui.

Banking System

- China's capital markets are dominated by a state owned banking sector that generally channels funds to state-owned enterprises on the basis of public policy rather than market considerations. Other domestic firms must find different sources of financing, including direct investment, gray-market sales of stock, and borrowing from other firms or non-bank institutions.
- Foreign firms that need working capital, whether foreign exchange or local currency, may obtain short-term loans from China's state-owned commercial banks. However, priority lending is often given to investments, which bring in advanced technology or produce goods for export. China's banking system is changing rapidly under the impetus of economic reforms.
- Foreign branches are generally prohibited from accepting RMB deposits but can maintain RMB accounts to provide foreign-exchange conversion for their customers. China has pledged to expand the scope of renminbi business gradually and to eliminate geographical restrictions.
- The Central Bank – The People's Bank of China (PBOC) – sets monetary, and with the State Administration of Foreign Exchange (SAFE), foreign exchange related policies. The People's Bank of China (China's central bank) reorganized its regulatory structure in 1998, and announced plans to set-up asset-management companies to take over the bad loans and help the commercial banks meet international capital adequacy standards.

[2] FIEs = foreign-invested enterprises, including foreign/Chinese equity joint ventures, cooperative or contractual joint ventures, and wholly-foreign-owned companies

Securities Markets

- The development of China's domestic capital markets has not kept pace with the needs of the economy, but two stock exchanges have been established in **Shanghai** (in November 1990) and the city of **Shenzhen** (July 1991) in southern China's booming Guangdong Province.

- Other regional "securities exchange centres" have had their ups and downs and were recently closed by the newly established **China Securities Regulatory Commission** (CSRC). A Securities Law was finally passed in late 1998 (to be implemented in 1999). Despite the tougher penalties for insider trading and other forms of fraud, the CSRC's lack of experienced personnel and the need for China to adopt and enforce international accounting standards remain major problems.

- Although in theory FIEs may apply for permission to raise capital directly on China's stock and bond markets, the approval process is not transparent and permission is practically impossible to obtain. (Capital costs tend to be higher in China than elsewhere, so many FIE's prefer to use offshore funding sources.). There are restrictions on foreign brokerages underwriting local currency shares (A shares), and foreign-invested brokerages must restrict trading to foreign currency shares (B shares) that make up a tiny fraction of the market. Much of the regulation and permissions to foreign investors happen on a case to case basis.

Foreign Exchange and Convertibility

- Since 1994, however, China's foreign reserves have grown rapidly (exceeding $146 billion by mid-1999), and FIE's have generally enjoyed liberal access to foreign exchange. China announced full convertibility in the current account in December 1996 and implemented new, liberal measures that allow foreign investors to freely convert currencies for trade and profit-repatriation transactions. <u>Capital account transactions remain controlled</u>. China's goal of achieving a fully convertible currency by the year 2000 has been pushed back because of the Asian financial crisis.

- The People's Bank of China (PBOC) and the SAFE regulate the flow of foreign exchange in and out of the country, and set exchange rates through a "managed float" system. China also has a very bulky exchange control regulations.

Infrastructure

- Lujiazui Finance & Trade Zone, demonstrates China's efforts to construct a financial centre in its own backyard. 1.6 million square meters of old buildings have been demolished, 1.72 million square meters of land have been cleared, and 1.16 million square meters of new houses for the relocated have been put up. Excellent planning and urban infrastructure being established on the lines of international standards.

  Altogether, 20,122 households and 532 enterprises have been relocated. The scale of the relocation work is equivalent to that of shifting a moderately large town. The urban landscape has been entirely changed after 7 years of construction activity.

Weaknesses

- Certain weaknesses with China remain. It is still a relatively highly regulated environment. Concessions attracting sometimes have to be negotiated with the authorities and may not be automatically conferred.

- The capital costs in China are high and there is a preference for offshore funding of investments to the extent permitted. There is restricted convertibility on the capital account while current account is freely convertible.

Conclusion

Low cost location
Competition to Hong Kong

Still a long way from being a regional financial centre

While Lujiazui is at present a relatively lower cost location among existing financial centres in Asia, it will take time to gain significant business volumes. The Chinese authorities intend to follow a clear and focussed action plan in converting the centre into an important regional financial and later an international centre. With the entire Chinese economy to ride on, Lujiazui has a right backbone for the planned transition. Initially, Lujiazui initially hopes to make significant gains partly at the expense of Hong Kong. If Chinese authorities persist with their experiments of economic liberalisation in Lujiazui, it could well become another attractive trade and financial services base in Asia.

6. Advantage India

How is India placed vis-a-vis other centres to become a regional financial centre? India with its top-ten growth economy status, a growth fuelled by knowledge sector, its large domestic markets and good geographical location, is ideally placed to become a financial centre of repute.

One of the top ten growth economies in the world

✓ India is one of the top ten growth economies of the World with large requirement of capital in areas of infrastructure and manufacturing as well as the newer technology related areas.

✓ India is a well-functioning democracy India has a stable politico legal system and broad consensus on reform policies, which are essential for attracting capital in the financial sector.

Poised for knowledge fuelled growth in the real sector

✓ Indian economy is well poised for growth, especially in the knowledge-based sectors of IT, telecom, media and biotech areas, which are likely to attract substantial investment. The growth in knowledge sector will create a need for a whole range of financial services and products.

Large domestic markets

✓ The presence of a large domestic market, is a favourable ingredient for the development of a financial centre. As discussed above, India with its large requirements in the infrastructure sector and a growing new economy with its requirement of new and complex financial products provides a large domestic market for the financial centre.

Advantageous Geographical location.

✓ India is geographically well placed between the centres of the South East Asia like Hong Kong and Singapore and the centres of Europe, Frankfurt and London.

Availability of skilled workforce

- ✓ Availability of skilled workforce in the financial sector and allied services like accountancy and law, along with the knowledge of English, also gives India a significant advantage, vis-a-vis other countries.
- ✓ The advantage of working in private sector also gives India, a advantage vis-a-vis countries like China which has a dominant state sector.

6.1. Issues to be addressed ...

State of Financial Reforms

- ❖ Reforms in the Indian financial markets began in earnest only in the early 1990s. Various sectors were delicensed and deregulated. The first steps toward strengthening the banking system, equity and debt markets were taken. Private participation was allowed in all financial sectors except in the insurance sector, which was the last sector to be opened. However due to the late start and slow pace of reform measures India still lags behind her many of peers in the region, as an open attractive destination for foreign investment.

6.2. Conclusion

India has the key ingredients for development of a regional financial centre with a reasonably big and fast growing economy. Moreover, the future knowledge fuelled growth in the Indian economy provides a right platform for development of the financial centre. The development of a financial centre in India is also aided by the advantageous geographical location and availability of skilled workforce. However, in order to become a more attractive destination for foreign investment, India would need to increase the pace of reforms in the financial sector, especially the capital markets and reduce the various levels of controls on the financial system.

7. Why Mumbai as a Financial Centre

Why Mumbai over other locations in India? The city, in spite of its infrastructure problems, has amongst the best reasons going for it to fulfil the regional financial centre role envisioned.

7.1. Advantage Mumbai

Clustering of Financial institutions / Market Participants

- ✓ Mumbai is the centre of Indian Banking and Financial Services activity. Majority of the big banks, financial institutions and investment institutions are based in Mumbai. Moreover other investors like mutual funds and private equity financiers are also based in Mumbai
- ✓ Over 9000 brokerages operate on the main stock exchanges, a significant number of which are based in Mumbai. There are also close to 500 foreign institutional investors (FIIs) and 800 merchant banks registered in India, most of which are again based in Mumbai. Even after the advent of automated trading and regional settlement, Mumbai retains most members given the large presence of retail investors with high savings rates.

Centre of Markets

- ✓ The main stock exchanges (BSE and NSE) and the debt markets are based in Mumbai. While India is not a hub for foreign exchange, such as the Asian Dollar Market in Singapore, treasuries of banks dealing in foreign exchange are headquartered in Mumbai, and most interbank currency dealing occurs out of Mumbai.

Highest concentration of skilled workforce

- ✓ The establishment of many corporate headquarters in Mumbai has attracted a high concentration of talent into Mumbai. A significant number of MBAs, chartered accountants, legal advisors and research professionals are based in Mumbai. So, Mumbai represents a destination for shifting activities, such as legal, global research and production departments to India in the medium term, if costs justify the same.

Centre of Trade and Commerce

✓ The presence of two major ports, Mumbai port trust and Nava Sheva Port will continue to ensure the domination this region has in the international trade and exports. Mumbai is the centre of trade and commerce in the country. Mumbai also serves as the headquarters for many companies and is also the busiest port in the country. The leading position in trade and commerce gives a ready market for the financial services on offer in an international financial centre.

7.2. Issues to be addressed ...

High cost location

❖ Mumbai has already gained the reputation of being a high cost location to establish operations in. Most FIIs set up base in Mumbai due to proximity to the markets complaining about the extremely high rental costs. However when it comes to establishing IT enabled services in India, corporations are by-passing Mumbai and surrounding regions, preferring other cities instead, such as Delhi and Chennai instead. Given the advancements in communication technology, Mumbai will have to guard from becoming a location that is too expensive and offers little exceptional benefit.

Strained infrastructure

Areas in Mumbai are clearly demonstrating the effects of a high rate of urbanisation. High population density, proliferation of slum dwellings and unorganised settlements, strained transport infrastructure are some of these effects. An emerging financial centre should plan ahead of the anticipated growth and should gear its administrative machinery to implement growth management plans. [3]

7.3. Conclusion

Mumbai is well positioned to pursue the regional financial centre strategy. To make this a reality the following steps need to be undertaken.

[3] An extract of some past reports on improving Mumbai's Infrastructure and urban development has been given in the annexure.

1. Identify a **strategic position for Mumbai as a regional financial centre**
2. Identify the **high profile financial service activities to be attracted to Mumbai** to capitalise on the growth
3. Ensure **coordinated working with local bodies and regulatory authorities to meet common objectives** which are

- ✓ Enable competitiveness in cost of establishment in Mumbai
- ✓ Undertake critical urban infrastructure and transport capacity creation / upgradation on a war footing
- ✓ Develop financial markets for greater sophistication

8. Positioning Mumbai

As discussed in the initial chapters, the following factors have contributed to the creation of successful financial centres in the past.

e) Consolidation of a first mover advantage as a key trading centre
f) Domestic demand for high quality financial services arising from the hinterland or from being a critical centre for trade and industry
g) The offshore / "tax haven" model
h) Cost effectiveness as a financial services location

While Mumbai clearly has had a lead within India, a larger role as a financial centre in the Asian region is a more difficult proposition. The real sector in India is witnessing growth in certain areas. This includes the ***IT/Media/Entertainment/Telecom Sector*** and the ***Infrastructure Sector***. While the former has been identified as an engine of growth, the latter cannot afford to be left behind, given the tremendous demand for infrastructure services. Growth in these sectors will draw upon sophisticated financial services and large volumes of funds both from India and abroad.

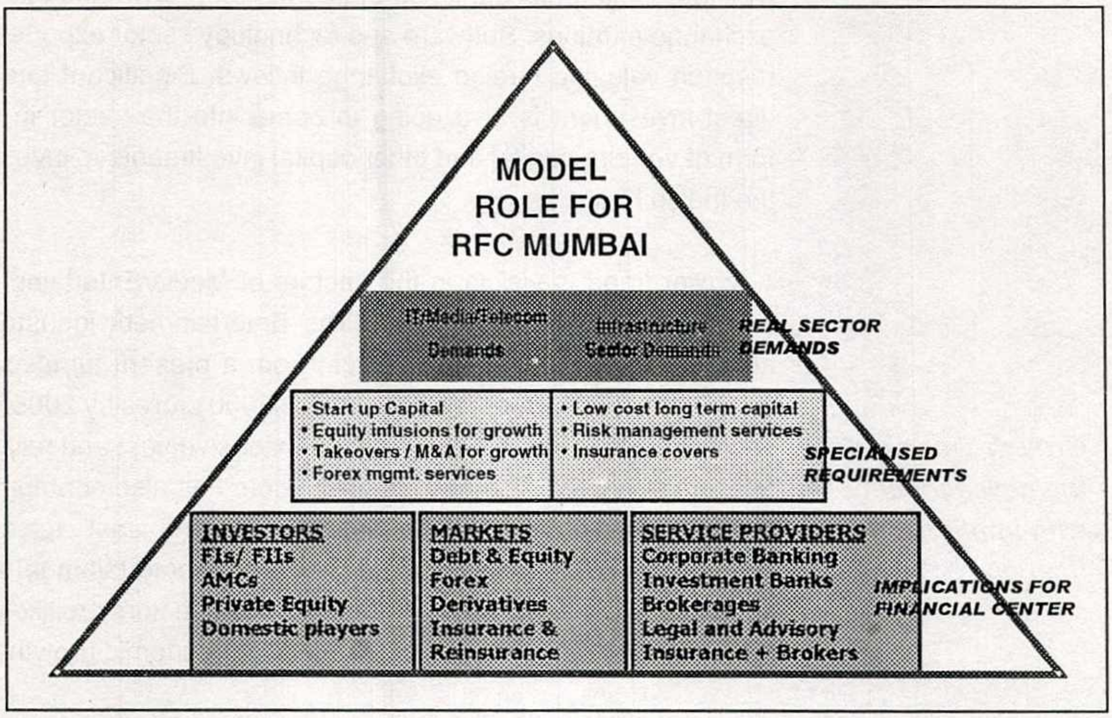
Thus the Financial Centre Mumbai should aim at

a) Attracting financial business associated with these sectors in India

b) Attracting providers of required financial services

c) Exporting skills over the long term to other centres

9. MODEL ROLE FOR RFC MUMBAI



9.1. Real Sector Growth Drivers – The IT/Media/Entertainment/Telecom sector (The New Economy)

Growing IT/Media/Entertainment and Telecom sectors

The recent growth in India and for that matter across the world has been largely fuelled by the growth in the so-called "New Economy" sectors. The constituents of the new economy, namely the sectors of IT/Media/Entertainment and Telecom are highly dependent on each other and create a lot of synergies among one another. The growing requirement of investment in these sectors as well as transborder consolidations and mergers is likely to provide a large market for the financial services sector.

A recent report by McKinsey & Co. For NASSCOM has indicated gross revenue potential from the information technology (IT) sector in FY 2008, of **USD 85 bn.** From the present **USD 3.9 bn.** (FY 1998-99). This will be possible if India capitalizes on its advantages. IT is being recognised by different countries in Asia as the engine to revive their flagging economies, much the same way that India today banks on the sector for growth and foreign exchange earnings. Software and technology sector exports will result in valuable foreign exchange inflows. Significant foreign direct investment is also going to come into the sector in the form of venture capital and other capital investments to invest in the Indian IT story.

Growth Trends in the new economy with implications for financial activities

A similar trend is visible in the sectors of Media/Entertainment and telecom Industries as well. The Entertainment Industry is also poised to grow at a fast pace, from a present turnover of around Rs 15000 crores (1999), to Rs 65000 crores by 2005[4]. IT sector growth is highly dependent on extensive, fast and reliable telecom services. The new internet boom has also contributed to the requirements of a dependable and fast telecom infrastructure along with lot of requirements of entertainment and media software to provide content. All these sectors are likely to grow at a fast pace and would lead India's economic growth.

However the projected high growth rates cannot be achieved through organic growth alone. There is bound to be a massive wave of globalization of the sector, including overseas mergers and acquisitions, setting up subsidiaries, company or branches in other countries to provide better services and movement up the value chain. Indian software companies are already beginning to increase their local presence on a worldwide basis. Currently, 203 Indian software companies already have either subsidiaries or branches overseas, mostly within the US. Their proximity to those markets helps them anticipate market conditions and client requirements, in addition to strengthening relationships and build partnerships. Indian software companies have gained a strong foothold in Software Services, E-Commerce, IT enabled services and ERP applications. Recently there have also been similar activities in the Telecom sector with both Public sector telecom players MTNL and VSNL planning NYSE listing. Even the India entertainment sector has started synergistic consolidations with Zee Television taking a stake in International Satellite telecommunication (ICO).

[4] Study done by Arthur Anderson on Indian Entertainment Industry

Trends exhibited in the IT/ Telecom/Entertainment sector by Indian companies

- ✓ A number of **private equity funds, venture capitalists** and **angel investors** are assessing Indian E-commerce / Internet business plans /Entertainment software and other software technology plans in India
- ✓ **M&A activity / Takeovers of domestic and foreign companies** to reach economies of scale and diversify across markets and add synergies
- ✓ Growth strategies are being funded through the **issue of ADRs/GDRs as well as domestic issues. Listing of the same on international exchanges**

9.2. The Infrastructure Sector

Large infrastructure needs

The Indian infrastructure sector is in need of large volumes of finances. In most areas foreign capital is being sought as the domestic capacity to supply the required volumes of long term capital is inadequate. The "The India Infrastructure Report : Policy Imperatives for Growth and Welfare" (Rakesh Mohan Committee, 1997) puts the annual need for infrastructure financing in a wide range of sectors (urban infrastructure, ports, telecommunications, roads, industrial parks and ports) at Rs. 1100 billion per annum by FY2001 and Rs. 1800 billion to 2005-06 implying a total investment requirement of Rs. 11,000 – 12,000 billion in the period FY 1996 – FY 2006.

Need for foreign capital

While a large component of this would have to be domestically financed, a significant component of financing would come from external capital flows. India can only attract these flows through an open foreign investment regime in these sectors. Investments in base infrastructure are imperative for private sector initiatives in downstream sectors.

Channeling of domestic savings to fund infrastructure

To channelise domestic savings into the sector, equity and debt markets will have to enlarge significantly. Domestic savings will have to be increasingly attracted into long term savings instruments such as pension funds, life insurance and provident funds though a mix of returns and fiscal incentives. The developments in this sector would result in:

Potential financial services activities

- ✓ Total estimated fund raising to the tune of **Rs. 750 billion per annum** from the domestic capital markets.
- ✓ Channeling of funds from contractual savings institutions (LIC, GIC, PFs, EPFs) and the newly opened insurance sector
- ✓ Associated services of financial consultants, accountants, bankers, legal professionals etc. for project structuring
- ✓ Associated services of **insurance companies / re-insurance companies** for project risk management solutions.

9.3. Other Sectors

Public sector funds

There are other sectors where the scope for financial service activities is tremendous. Privatisation of **Public sector enterprises** has been regarded as a critical sectoral reform measure as well as a source of funds for the cash strapped governments. During the first round of disinvestment, the Government of India divested a small stake in various core sector enterprises to the public. However economic compulsions such as burgeoning fiscal deficits and limited financing avenues are forcing the government to proceed with privatisation on a larger scale. The Government privatisation policy is also directed toward bringing efficiency to the operations.

Privatisation of good state assets will attract hordes of investment bankers, brokerage institutions and retail asset managers and represents an opportunity for financial services to be transacted out of India.

Corporate restructuring

Corporate restructuring activity is also on the rise in India. Driven by globalisation, Indian corporates have been reorganising their businesses through acquisitions, hiving off units and through other means to achieve economies of scale or the focus that will enable them to become globally if not regionally competitive. These activities will require specialised advisory assistance on deal financing and implementation.

10. Attract Key Financial Services Providers to RFC Mumbai

The new economy sectors and Infrastructure financing activities provide an opportunity for Indian financial services companies to participate in. As discussed before Mumbai should concentrate on building a strong base in 4 to 5 key financial services segments which will aid these sectors. This section profiles the key issues pertaining to these sectors.

Sector	Critical for
Private Equity/ Venture Capital/	✓ Risk capital for IT, E-Commerce, Biotech and other risk ventures not financed by conventional banks ✓ Inflow of long term foreign capital to support India entrepreneurs
Financial Services Segment : Asset Management Operations	✓ Widening participation base in debt and equity markets. ✓ Professional Institutional fund management service for retail investors. May be accessed by PFs, EPFs, and Insurance companies when regulations permit.
Investment Banking / Broking	✓ IPO Management expertise of an increasing number of startups on the domestic exchanges. ✓ Advise on domestic leg of cross border M&A deals. Bringing international experience to domestic markets ✓ Research on Indian markets and companies to international investors.
Insurance	✓ Expansion of insurance markets and mobilisation of long term funds. ✓ Comprehensive infrastructure project insurance covers, which are not available domestically.
Offshore Banking Units	✓ Encouraging flow of foreign trade and investments ✓ Improved share of regional forex business and cross border banking ✓ Managing transition to capital account convertibility ✓ Important step towards development of financial centre

10.1. Private Equity and Venture Capital

Private Equity and Venture Capital : Increasing interest in Indian Technology sector.

In 1996, the *Securities and Exchange Board of India* (SEBI) came out with guidelines for venture capital funds activities in India. The move liberated the industry from a number of bureaucratic hassles and paved the path for the entry of a number of foreign funds into India. Increased competition brought with it greater access to capital and professional business practices from the most mature markets.

The Venture Capital (VC) industry in India consists of offshore and domestic funds. Offshore VC funds usually invest a minimum of US $ 1 million and cater to established players with large requirements. Domestic VC funds constitute a minority at present and usually cater to small scale start-ups.

In addition to the organized sector, there are a number of players operating in India whose activity is not monitored by the Indian Venture Capital Association. Add together the infusion of funds by overseas funds, private individuals, 'angel' investors and a host of financial intermediaries and the total pool of Indian Venture Capital today, stands at Rs. 50 bn. (in excess of USD 1 billion), according to industry estimates.

Issues concerning the Private Equity / Venture Capital Industry

Relatively new development

Till early 90s, under the license regime, only commodity centric businesses thrived in a deficit situation where venture capital was not required. Most of these entities were capable of raising funds from conventional sources, including term loans from institutions and equity markets.

Secondly, as most initial venture capital units were offshoots of financial institutions and banks they continued to want to provide capital on a secured debt basis, to established businesses with profitable operating histories.

Regulations

There are a multiplicity of regulators, like SEBI and RBI and the CBDT. Domestic venture funds are set up under the Indian Trusts Act of 1882 as per SEBI guidelines, while offshore funds routed through Mauritius follow RBI guidelines. Internationally, such funds are made under the Limited Partnership Act, which brings advantages in terms of taxation. Present restrictions do not permit pension funds and insurance companies to invest in venture funds as in USA.

Limited Exit Options

The exit routes available to these categories of fund providers were restricted to the IPO route. Given the failure of the OTCEI and the revised guidelines for listing, small companies could not hope for a BSE/ NSE listing. Even the market for mergers and acquisitions, strategic sales were limited.

VCs also rely on buyback clauses with the promoters.

Conclusion

The Private/Equity/Venture Capital pool in Hong Kong is 5.5% of the country's GDP, with similar figures in Singapore and South Korea. In India, the pool size if far lower at 0.5% of GDP. However this funding source has certain advantages such as

- Longer term foreign investment than normal FII investments
- More management oriented approach to investment
- High projected investment growth rates in India

This sector provides an attractive opportunity for Mumbai to capitalise on. The different regulators have to operate in close coordination while evolving regulatory guidelines and frameworks, to ensure that common objectives, such as shifting of a larger base of venture capitalists, to India are met.

Venture Funds for India

The IndUS Entrepreneurs (TiE), a networking society that brings together highly influential Indians across the US was set up in 1992. The aim of the organization is to get the community together and to foster entrepreneurs and wealth creation. The idea was sparked off in 1992, when a group of Silicon Valley entrepreneurs with roots in the Indian sub-continent met by chance for a meeting with a visiting dignitary from India. A delayed flight kept the group waiting, and provided an opportunity for people to get to know one another. It turned out that most of the assembled invitees to the meeting had achieved varying degrees of entrepreneurial success. The group saw value in getting together on a regular basis to network with one another. Thus, the idea of TiE was born as a mechanism for high achievement-oriented IndUS entrepreneurs to network.

Over the years, a core group of about 10-15 individuals worked hard to establish the organization. Meeting at least once a month, successful veteran entrepreneurs, contributed as speakers, participants and mentors. Gradually, the group started attracting greater participation, and the TiE concept started gaining momentum. TiE membership has now grown to over 600 members, and chapters in Boston, Austin and Los Angeles. TiE is also supported by over 20 institutions that include leading Silicon Valley venture capital investors, law firms, accounting firms and banks.

10.2. Foreign Institutional Investors

FII Investments, a large untapped potential.

FIIs in India are regulated by SEBI. FIIs are primarily into market operations (equity and debt). There are over 200 FIIs in India based mainly in Mumbai accounting for a total investment of $. 11.8 billion (April 2000) which is routed through offshore bases. This amount has shown a consistent increase over the last 3 years.

Allocation dependent on macro-economic and political factors

FII investments into India come from the 'India Fund', dedicated to making investment in India and other funds earmarked as 'Regional Funds' (such as Asia Fund), 'Emerging Markets Fund', 'Global Fund', 'Index Fund' and 'Hedge Funds'. And in all these, Indian companies get a flexible share, which rise and ebb based on the economic and political factors prevailing in India. India gets a 2% - 3% allocation from the 'Emerging Markets Fund'. Its share can rise to 7%-8% bringing in additional investment in the order of a few billion USDs, if certain systems and policies are streamlined.

10.3. Foreign financial services institutions

In the financial sector, foreign financial service institutions are allowed to set up joint ventures in stock broking, asset management companies, merchant banking and other financial services firms along with Indian partners. At present the maximum holding of the FII is restricted to 75%. The foreign participation in financial services requires the approval of Foreign Investment Promotion Board (FIPB) to bring in FDI for participation.

Participation guidelines

100% investment in Indian subsidiaries: Foreign investors are not allowed to own 100% subsidiaries incorporated in India in the financial services sector. There is a maximum limit of 75% of the equity capital.

Investment Servicing

Repatriation of Income: Dividend is the main form of repatriation to FIIs foreign stakeholder. While repatriation of dividend income has been streamlined, a dividend tax of 11% is being levied on the distributed profits. This is significantly higher compared to other financial centres.

Taxation rates

Investment Banking: Most cross border transactions involving Indian companies occur through a branch outside India. This is on account of the high taxation rates (effective rate of 48.5%) on foreign companies in India. As a result bulk of the income on this type of activity is booked abroad. Singapore on the other hand has a lower rate of taxation for cross border financial activity that is underwritten from Singapore thereby encouraging more of this activity to take place in Singapore.

Remittance of Fees: Companies operating in India also face problems in remitting legal and advisory fees to their international partners. As a result, significant part of the income from cross border activity is booked abroad.

In the case of foreign brokerages, there are restrictions on the reimbursement of fees for the preparation of international research and production activities pertaining to the Indian markets. Presently expenses incurred internationally by international sales, marketing and production teams on domestic products are borne out of international offices.

Conclusion

At present hub activities of international financial institutions are mostly based in Singapore or Hong Kong. Many of the important positions are also occupied by locals. Moreover, the top management professionals enjoy an excellent quality lifestyle at these locations. Given these facts, shifting hub operations to India presents a challenging task. However, this is precisely what, Mumbai would need to focus on, namely, attracting the **hub activities of Indian and Regional** financial services institutions planning to establish operations in Asia, for emerging as a prominent RFC.

10.4. Insurance Sector

Still in Shackles...

Given the long term nature of insurance business, few domestic private sector players can be expected to participate, especially in the initial years. No financial returns can be expected to accrue in the initial 5 to 8 years. Besides, even after this period dividend would be limited by regulators to not more than 10 per cent.

Excluding India, Myanmar, North Korea and Cuba are the only countries where foreign insurance companies are denied entry. China opened up its insurance business to foreign companies about a decade ago. Over 28 foreign companies operate in the Chinese insurance market.

Foreign investment companies have large investments in USA, UK, EU and Japan where the regulators permit investment of funds abroad. Foreign participation in Indian insurance can therefore facilitate flow of funds to infrastructure sector as the insurance funds have a reasonably long tenor to meet the needs of high gestation infrastructure projects.
Experience in Asian countries has been encouraging in terms of growth in premium and employment. Joint venture with foreign equity participation would facilitate utilisation of foreign funds and expertise in the development of a wide variety of insurance products at low costs.

Participation guidelines

The decision to open the Indian insurance business to private sector implies foreign participation by joint ventures also. The main highlights are:

- Insurance Regulatory and Development Authority (IRDA) allows foreign participation through JVs with a maximum participation of 26% of equity stake by the foreign participant. Separate life and non-life licenses to be issued. Minimum seed capital of Rs. 100 crore.
- RBI allows Indian Banks / FIs to participate subject to minimum net worth of Rs. 500 crore, NPA caps and a maximum participation of 30%. These regulations may be reviewed.

JV Management Issues

The impact of these initial participation guidelines is yet to be seen. However it can be clearly noticed that there are likely to be more than 2 parties within the Joint Venture forming the insurance company. Most banks would be excluded as partners on the basis of the present RBI thinking on participation in the sector. Managing the JV smoothly through the initial turbulent phase is likely to be a critical issue.

Conclusion

Mumbai has an advantage in attracting insurance sector as most of the potential JV participants are already established in the city. Mumbai and Maharashtra also form an attractive market to target in the initial period of operations. However, Mumbai's disadvantage is the fact that the Insurance Regulatory and Development Authority will be based in Delhi.

11. Develop Domestic Markets

11.1. The Stock Exchanges

Stock Markets: Comparable to other Asian markets, but lack width and depth

The Indian equity market at present has an estimated market capitalization of $ 230 billion, which is comparable to most of the other markets in the region with the exception of Japan. The liquidity and depth in the markets have shown significant improvement over the last 2 years especially after the securities scam in 1993-94. However among the main players, foreign institutional investors, brokers and asset management companies the market is still controlled to a large extent by the first two entities.

Strong financial markets are the pride of the financial centres of international repute. These markets have become significantly developed on account of catering to a wide base demand from the domestic environment. Today markets such as NASDAQ and New York's NYSE are listing both international debt and equity offerings. Europe's equity markets are also undergoing a phase of consolidation.

Regulation

- The Securities Exchange Board of India (SEBI) regulates the stock markets. SEBI also is responsible for gradually removing restrictions on markets activities as well as controlling them. SEBI has in the past introduced stop gap measures, such as the temporary banning of short selling in June 1998 on account of high market volatility following imposition of sanctions by US.

Dematerialisation :

- Among the milestones reached by the Indian equity markets, the introduction of dematerialisation of scrips in a phased manner has been a significant development. As of February 2000, over 750 companies had signed dematerialisation agreements with the main depositories. This has improved the liquidity in the markets by enabling large-scale retail level participation.

Investors have suffered on account of fraudulent paper entering the market during the dematerialisation process, which the legal system has not been able to sort in a quick and efficient manner.

Rolling settlement :

- Rolling settlement was introduced to curb excessive speculation on select scrips dictated by the regulator. However, there is also a risk that market making interest in a particular scrip maybe reduced thereby killing any speculative interest in the particular scrip which is responsible for injecting liquidity. To be operationally effective, rolling settlement need to be complemented with **electronic payment systems.**

  Rolling settlement is necessary for a healthy and safe market as it helps in reduction of risks and also lowering of transaction cost in the long run. Most international markets have moved into rolling settlement mould. However rolling settlement is ideally suited to forward / futures trading.

Other advancements

- **Other advancements** made in recent times include permitting companies to **buyback** shares (subject to various conditions) and also allowing companies to raise capital through the **bookbuilding process** (for issues greater that Rs. 25 crore.). These are positive and market friendly developments. **Infrastructure Companies** are also granted exemptions on the stock markets in terms of mobilisation and pricing.

Derivatives trading: Untapped potential

A derivatives market will be successful only if there is a strong market in the underlying asset. In the Indian market, most derivatives have been banned with a exception of a select few such as specific commodity futures contracts. The Cabinet in October 1999 cleared a bill that will pave way for equity derivatives by mid 2000.

Derivatives are present in any sophisticated market as they constitute an important risk management tools. Derivative positions may be taken up by various players such as domestic brokers, financials institutions and FIIs to hedge against adverse movement of their portfolios.

A derivatives market in equities will naturally be centred in Mumbai, as the stock exchanges themselves will be introducing these products. The FIRE (Financial Institutions Reform) project has identified the requirements for evolving a strong and sound derivatives market in the country.

Pre-requisites to start

Phased introduction of derivatives :

Equity derivatives can be introduced after market participants have acquired a fair degree of familiarity and comfort using more broad-based derivatives such as index based futures, which could be a starting point. This will have to be enabled by the Securities Contracts (Regulation) Act.

Sound regulatory mechanism :

- While SEBI will control regulation of the markets, there will also have to be a strong level of regulation exercised by the exchange itself. This will include systems of stipulated capital adequacy standards, minimum net worth criteria for participants, guarantee fund and strong margining systems.

Upgradation of existing stock exchanges :

- NSE is in the process of upgrading its infrastructure facilities, online trading and surveillance system and acquiring minimum number of well-capitalised members for derivatives trading.

Adequate risk management and control:

- While derivatives provide and opportunity to hedgers, it is possible that the misuse of the instruments can lead to loss of market integrity. Effective control of derivative operations can be achieved through
  - Monitoring and dissemination by the exchange of information about the trades, quantities and quotes in real time.
  - Well-capitalised clearing corporations to guarantee both legs of every trade and have adequate backup systems for the same (i.e. daily margining system, guarantee fund etc.)
  - Stringent entry norms for clearing members in terms of capital adequacy, and refundable deposits.

Financial Derivatives :

- Financial derivatives such as interest rate swaps were introduced after much delay only in 1999. Interest rate swaps (IRS) are important tools for executing asset liability management strategies. The RBI had delayed the introduction on account of a poorly developed term money yield curve, which could effectively hamper pricing of these products. IRS has since then been introduced and transactions between banks and financial institutions are gradually picking up in volumes.

Conclusion

Fast liberalisation is a must

An active securities and derivative market is critical for a sophisticated financial centre. Indian markets are evolving at a gradual pace aided by gradual financial reform. However, with increasing globalisation. it is important for regulators to liberalise these markets fast, so that they may evolve as dominant markets in the region in terms of depth, sophistication.

Money markets : Lack maturity

11.2. Money Markets

This money market includes call money, notice money, certificates of deposits and other short-term monies. This market is presently unorganised in nature and most trading activity is conducted between banks on a daily basis. Recent improvements include the development of **MIBOR** (*Mumbai Interbank Offer Rate*), a benchmark rate for 3 month domestic interbank borrowing rates but little placement occurs on the basis of the benchmark.

The lack of liquidity

- There is little liquidity in the term money market for longer maturities than the overnight rate. Very few participants are willing to take a view on the level of interest rates for these maturities. The root of the liquidity problem lies in the following factors.

High volatility of the overnight rates (call rates)

- Participants unwilling to take a view on the term money market

Limited number of players

- Mutual funds and insurance companies are allowed in the money market segment. Therefore there are few players in the money market segments as a result of which there is limited liquidity.

Different instruments of different maturities

- Absence of money market instruments of varying maturities and the non-tradability of term money market investments

Setting of benchmark rates

- The market has to be developed through the setting of possible benchmark rates for term money transactions, which may then be disseminated on a wider platform. It is necessary that the current online exchanges become the preferred model of trading term money.

An approach suggested to setting benchmarks is the volume weighted average of all exchange traded deals (NSE/BSE). For this, a significant volume of deals should be done through the NSE online system. Currently, however, most of the term money market deals are done **over the phone**. Polling quotes from the participants and disseminating this information may aid in setting up benchmark rates.

Conclusion

It is important that a screen based systems of quotes for the funds market is developed to bring in transparency into the term money market. The Vaghul Committee as well as the Sodhani Committee, 1995 had recommended various measure on developing a term money market in India. The real impetus for money market development will come only after a mechanism to set accepted benchmark rates is introduced.

Term money markets

Knight Ridder has a specific page dedicated to interbank deposit rates (bid and offer) for the following maturities - overnight, 1 week, 2 week, 1 month and 3 month. Although there are 8-10 contributors for the overnight rate, for all longer maturities quotes are available from 3 banks only. (The regular contributors are Amex, HDFC Bank and Deustche). The bid-offer spreads also widen with maturity and for the 3 month maturity, it is as high as 2-3%, indicating the illiquidity at that maturity. The quotes are not provided for any specific amount. They are usually updated 2-3 times a day, based on availability of quotes from the banks.

Reuters originally provided a page with term money quotes from a few contributors but the same has been discontinued now. Currently, term money quotes are available only on the pages hosted by individual banks (specific to that bank).

11.3. Debt Markets

The Indian debt market comprises of government paper (Gilt) and corporate bonds. A developed debt market provides access to debt of the required duration at reasonable and market determined costs. It also provides investors a fair degree of liquidity to enter and exit their investments at reasonable cost. Though the Gilt market is mainly a telephone market, there has been growing liquidity in this market over the last few years encouraged by the gradual interest rate deregulation and the RBI's mark-to-market investment accounting requirement for banks. An increasing volume of the market has been moving to the NSE online system. Corporate debt instruments with over 18 months of initial maturity are mandated to be listed on the NSE online system.

Issues concerning Indian debt markets

Indian debt markets are characterised by lack of depth and liquidity, which are required for efficient operations. The challenges facing our debt markets are Under the present regulations selling short is not allowed.

Wider participation base

- Liquidity in the government securities markets can be further improved by permitting a wider base of players (e.g. satellite dealers, mutual funds etc.) to participate. Currently there are only 10 primary dealers and five satellite dealers. While improving institutional infrastructure, i.e. strengthening the primary and satellite dealers network and systems, it is also important to establish a wide retail network. Opening up the repo market to a wider base of participants will also enhance liquidity.

Poor liquidity in secondary corporate bond market

- The secondary bond market in India is underdeveloped. There is very little trading activity in secondary markets for any paper listed below 'AA-' credit rating as credit spreads become very difficult to estimate for lower ranked categories.

Weak bankruptcy laws

- Indian bankruptcy laws offer little protection in practice to the lender. Defaulting cases get resolved after enormous delays once they enter the ambit of the Sick Industrial Companies Act (SICA), 1985. While the Board for Industrial and Financial Reconstruction (BIFR) various proposals for turnaround of sick companies, lenders are subjected delays in recovery of principal as well as other business risks such as environment and policy changes.

  With the increasing level of financial reforms, the reconstruction of companies should be left to the capital markets, enabling lenders to recover dues without extended delays. This will have a positive impact on the development of high-risk debt investors such as junk bond investors.

Low level of Institutional development

- **Debt recovery tribunals** (DRTs), suggested as an enabling measure to recover overdues of banks focus on enabling. The performance of the tribunals has been unsatisfactory so far with just less than 5% of dues actually recovered. The DRTs, are overloaded with cases with inadequate legal staff to take on the proceedings.

Credit information bureaus

Credit information bureaus play an active role in disseminating information among lenders about the credit quality of counterparties. While the RBI has set out with an objective of creating credit information bureaus and enabling the circulation of negative lists among lenders, the scope has to be widened to include both business as well as the retail sector. Changes in the Banking Secrecy Act may have to be considered to enable the smooth functioning of credit bureaus.

As a result of the above factors the medium to high risk bond market in India has suffered in terms of development. This also poses a stumbling block for the development of more complex instruments such as credit derivatives.

Conclusion

It is important for the markets to establish a transparent and credible price discovery process in the primary market and develop a vibrant, liquid and broadbased secondary market. At the same time it is important to constantly enable more sophisticated instruments and transactions on the market while at the same ensuring a smooth, well functioning and efficient dealing and settlement system. The absence of short selling of securities on the debt markets is one such measure that impedes effective operations of operators.

With the opening of the insurance sector, to private sector participants there will be greater number of players in the debt markets. Secondly management of EPFs (Employee Provident Fund) by professional AMCs will also bring a wider number of securities under active management. Other reforms such as permitting new private and public provident and pension funds and relaxing investment guidelines will have positive impact on the debt market evolution.

12. Offshore Banking

Offshore Banking would provide the ideal impetus to RFC Mumbai.

The ability to conduct offshore business is an important component of any aspiring financial centre. Financial centres in Asia where exchange controls still prevail usually allow offshore banks to operate in a controlled manner. The Sodhani Committee (Expert Group on Foreign Exchange Markets in India 1995) had recommended the establishment of an Offshore banking centre as a phased plan to achieving integration of India's market with the world markets, i.e. the stage when India allows convertibility of the rupee on the capital account.

Setting a geographically bound offshore banking centre in Mumbai governed by a separate legislation will provide the ideal impetus to the development of RFC Mumbai. This can be done on a restricted basis much in the same manner adopted by Singapore before the island nation adopted capital account convertibility. In Singapore, CAC was introduced only recently following a significant period of conservative approach to exchange controls. At present it is freely convertible for residents and non-residents. Overseas investments are encouraged and so are offshore investments using Singapore as a base. Singapore was a recognised offshore banking centre well before capital account convertibility was allowed. The main principle of the offshore centre in Mumbai are

- Clear segregation of offshore and onshore activities to enable regulatory control
- Giving licenses for offshore business to only existing reputed commercial banks in India meeting stringent capital considerations (to protect the banking system)

NRI money – the key source funding offshore banks

Funding Sources

The main sources of funds for offshore banks in India would be foreign currency deposits from NRIs.

- Funds can be sourced from foreign entities and other foreign branches of Indian banks through the issuance of foreign currency CDs.
- Deposits from residents eligible to hold foreign currency accounts such as EEFC. Though strictly not foreign in source, this will increase quantum of funds that are free of reserve requirements, which will improve liquidity and pricing more in line with international rates.
- Deposits from other Offshore banking units in India

Foreign currency loans to fund infrastructure products.

Deployment Avenues

- Lending in foreign currency to non-residents and other offshore banking units
- Investments in specific categories of assets permitted by RBI
- Lending to entities in foreign currency for infrastructure project finance which at present depend on FDI alone for external funds

Fee Based activities and trading

Other activities

The Sodhani Committee reports also recommends that

- OBUs should be allowed to undertake fee-based activities such as foreign currency trading with authorised dealers (excluding domestic currency), non-residents and other offshore units.
- Issue **guarantees** not involving domestic currency / local exposure
- **Foreign currency loan syndication** for loans raised abroad or booked in their own books
- **Opening, advising, negotiating** and **confirming LCs in foreign currencies** where both the parties are non-residents.

Separate act to regulate off shore centre.

Minimum necessary regulations

A separate **Offshore Banking Act** will have to be enacted, under which OBUs will be regulated. While liabilities of OBUs will be exempt from local reserve requirements (to allow pricing in line with international levels) RBI can specify minimum liquid assets. Concessions will have to be negotiated with the CBDT to ensure that Income tax rates are comparable to that of other surrounding destinations. Withholding tax exemptions on interest income of non-resident deposits will definitely enable business volumes to grow. However nominal tax should be effected. Also the units should be exempt from stamp duty for transfer of loans and other activities. Setting up an offshore centre is an important step in the smooth transition to capital account convertibility.

13. Evolution of RFC Mumbai

Given Mumbai's current advantages, its ability to attract capital and play a large role in the regional financial business, depends on three main factors

- The relative state of financial liberalisation in India
- Total quality adjusted cost of establishment in Mumbai
- Provision of good quality public education

Reforms in financial sector

The **state of financial liberalisation** is mainly a function of the Government of India's policies to attract investment into India and permit competition in key sectors. This is a gradually evolving process and Mumbai's ability to influence the speed of reforms are limited. This also determines business potential on the basis of which foreign financial services providers decide to invest in India.

Reduction in establishment costs

The reduction in **costs of establishment** of the extent of operations based in Mumbai is key to attract new services to be based in Mumbai. If the service provider only wishes to locate lower value, high workforce intensive operations in India, Mumbai's chances of attracting the same will be far lower. In the case of strategic level operations, Mumbai will be a natural choice. Mumbai will be benchmarked against Asian competitors not only on costs but also on the quality of infrastructure. Poor quality infrastructure in Mumbai will add a cost equivalent to Mumbai's already high costs.

Provision of good quality public education

Public education is another key area to be addressed by the State Government. There is a need to improve the education infrastructure across all levels, from primary education to setting up of specialised institutions. Provision of good quality public education is necessary for a constant supply of skilled workforce for the financial centre.

Conclusion

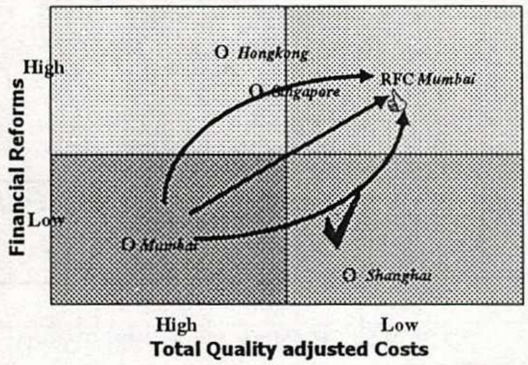
The State Government should focus on creating the right infrastructure amenities and pushing forward reforms to reduce costs of establishment. The state government should also work to improve public education, so as to maintain a good supply of skilled workforce for the financial centre. While the State Government may work with the Central Government and Regulatory bodies on urging financial reforms, this may take far longer in reality

Global Top 20 Index (Occupation Cost in USD / Sq. Ft./ Annum)					
1	Tokyo (Inner Central)	146.87	11	Edinburgh	57.92
2	London (West End)	131.94	12	New York (Mid Town)	56.14
3	Tokyo (Outer Central)	130.55	13	Birmingham	53.90
4	London (City)	104.59	14	Manchester	53.02
5	***Mumbai***	***76.04***	15	Glasgow	52.29
6	Hong Kong	70.39	16	Buenos Aires	50.17
7	Moscow	67.22	17	Dublin	49.99
8	Seoul	63.62	18	Taipei	49.63
9	Paris	62.57	19	San Francisco	48.51
10	Frankfurt	60.72	20	New Delhi	47.74
	Mumbai (BKC) *	***25***		***Mumbai (Andheri)****	***16.5***
Source : CB Richard Ellis : Global Market Rents : Jan 2000					
	** Colliers Jardine property trends : Jan 1999*				

Strategy for Mumbai

A long term strategy for the State Government in position Mumbai is shown in the figure (Evolution of RFC Mumbai).

Evolution of RFC Mumbai



1. ***Undertake measures to reduce the total quality adjusted cost of establishment in Mumbai through***

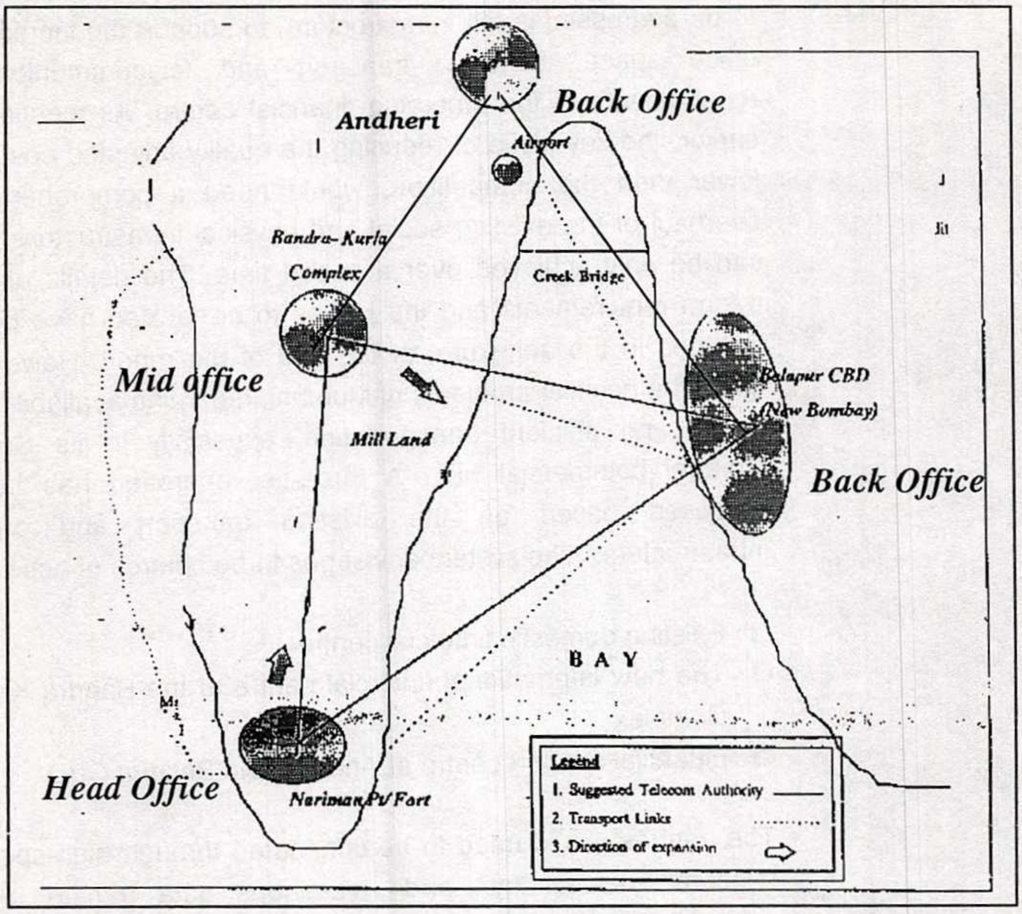
   a) improving city level urban infrastructure amenities
   b) removing constraints to improve office and residential space supply
   c) develop transportation links (internal and external)
   d) invest in developing satellite town outside Mumbai to curtail inward migration

   These measures will re-iterate commitment of state to attracting high value preferred sectors and services far better than a mix of state incentives from time to time.

2. ***Co-ordinate strategic marketing of Mumbai***
   a) attract domestic and regional headquarters of international corporations, and targeted international financial services organisations
   b) create and disseminate data on Mumbai and surrounding regions, financial sector players
   c) effort to retain high visibility projects involving FDI in the surrounding regions

3. ***Intensify efforts to consolidate domestic economic fundamentals.***
   a) restructuring towards knowledge-based and high valued-added activities
   b) jointly work with regulators and industry to carry through critical financial sector reforms and develop markets

14. Proposed Interim Office Location Plan



Source: *Bombay as a Regional Financial Centre – A Recap*
Presentation by Mr Girija Pande, ANZ Grindlays Bank

14.1. Introduction

Three-tier approach to office location

Besides the issue of reforms in the financial sector, the key area to be addressed is the infrastructure, to support the increased office space, housing, transport and telecommunication requirements of the emerging financial centre. As mentioned earlier, the key issue of reducing the quality adjusted costs to lower than the competition, would need a comprehensive overhaul of the existing social and physical infrastructure and can be only achieved over a period time. The details of the reform requirements and the issues to be tackled have been included in the annexure, at the end of the report. However, given the peculiar problems of Mumbai, regarding availability of space and efficient transportation, especially in its South Mumbai commercial hub. A three-tier approach has been proposed based on the existing transport and office infrastructure. The system envisages three centres of activity

- Existing domestic financial centre
- The new international financial centre at the Bandra Kurla Complex
- Financial support centre at Andheri and Belapur CBD

The centres would need to be connected through high-speed telecom links for fast and voluminous data transfer and connectivity. A fast and economical transport link for providing access to the financial centres and transport between these centres would need to be developed.

The Transport committee of Bombay First is working on a plan to remove bottlenecks and improve the transport infrastructure of Mumbai.

South Mumbai

14.2. Existing domestic financial centre: Corporate Offices

The existing financial centre would be left undisturbed and could serve as the headquarters of the existing financial institutions, financial regulators, the BSE, its brokers, other financial intermediaries, service providers and corporates.

1. Head office of commercial banks, FIs, Insurance companies
2. Regulators – RBI, SEBI, SROs (AMFI, AMBI, etc.) IRA
3. BSE
4. Brokers' front offices, SE & money markets
5. Investment Banks, Merchant Banks, Fund Managers
6. Existing Accountants/Solicitors
7. Large Corporate Head-offices
8. Clearing – Forex, Cheques

14.3. New International Financial Centre at Bandra-Kurla complex – Mid Offices

Bandra-Kurla Complex

The proposed new centre would accommodate some of institutions shifting from the high cost South Mumbai centres. It would also include the principal offices of the new banks, and some public sector banks, new insurance companies and other players. The complex would also accommodate offices of NSE, RBI clearing offices, etc.

1. Principal offices of new commercial banks
2. New Insurance and Brokers
3. Actuaries
4. OBUs/ International finance companies
5. Solicitors/ Accountants/Money & FX brokers
6. NSE
7. RBI Clearing centres
8. New Fund Managers

Andheri – Belapur

14.4. Financial support centre at Andheri and Belapur (CBD) – Back Office and Financial Support

The proposed financial support centre will accommodate the low value added activities and, space and manpower intensive support functions.

1. Depository/Custodians
2. Call centres
3. Back offices of banks, insurance and stock exchange brokers
4. Admin offices of FIs, research, credit department and audit department
5. Equity research firms
6. IT companies and computer support

Conclusion

This three-tier structure of office location would help in reducing the pressure on South Mumbai locations, which still houses a lot of workforce intensive and low value added activities. This will not only free up land for locating corporate offices of the new financial intermediaries, but also ease the traffic situation. However, effort in the area of improving housing and transport facilities close to the support centres of Andheri and Vashi-Belapur area would need to be undertaken. Efforts would also be needed to strengthen the transportation and communication infrastructure between the Axis of South Mumbai/ Bandra-Kurla/ Andheri/ Belapur.

Action Points

14.5. Action Points for to be taken up by various entities

Government of Maharashtra

- Key Initiatives to prevent dispersion to other centres
  - Provide cost effective infrastructure
    - Improve land & housing legislation - ULCRA, Rent Act
    - Increase FSI in Nariman Point
    - Free mill lands
    - Improve transportation links between the proposed hubs

- Rationalise stamp duty
- Lobby with Central Government to move pension and Insurance regulators to Mumbai

Ministry of Finance and RBI

- Rationalise legislation relating to Banking services
- Shifting Insurance and Pension regulators to Mumbai

SEBI

- Rationalise capital market legislations

MTNL/DOT/VSNL

- Improve telecom Infrastructure

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Sites of:

Hong Kong Monetary Authority

Monetary Authority of Singapore

Bank Negara, Malaysia

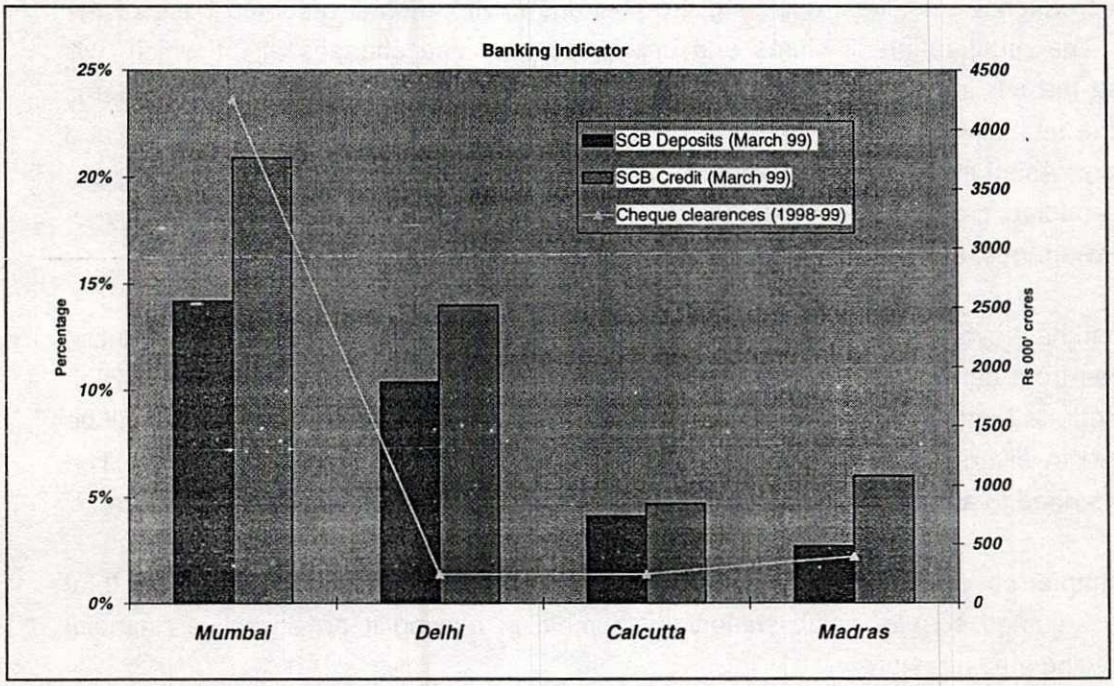
Taiwan Monetary Authority

ANNEXURE

1. Advantage Mumbai

Comparison of the four metros on select banking indicators

	SCB Deposits (March 99)	SCB Credit (March 99)	Cheque clearences (1998-99) (Rs000' crores)
Mumbai	14.2%	20.9%	4252
Delhi	10.4%	14.0%	247
Calcutta	4.1%	4.7%	247
Madras	2.7%	6.0%	396



2. Infrastructure and Urban Development

2.1. Urbanisation of Mumbai

The Economic Survey 98-99 points out that the shortage of employment opportunities in villages and ecological stresses are leading to increasing migration levels of poor families to towns. Mega cities are emerging and urban slums are expanding in an unplanned manner. During the past two decades of 1971-91, India's urban population has doubled from 109 million to 218 million and is estimated to reach 300 million by 2000 AD.

Urban development issues cannot be ignored in the process of attracting world class organisations to Mumbai. Accompanying a phase of rapid development is often lack of time and resources to plan urban infrastructure in a manner that supports the growth. This has widened the gap between demand and supply of infrastructure services such as energy, housing, transport, communication, education, water supply and sewerage and recreational amenities, depleting the precious environmental resource base of the cities. The proliferation of slums and unplanned land use changes all of which, will oppose the city's evolution to achieve its strategic role. Much of the deficiency stems from the financial arrangements that exist for investments in infrastructure renewal and addition. Asian tigers such as Bangkok, Manila or Mumbai have already borne the brunt of - unbridled growth on city infrastructure of traffic congestion, insufficient drainage, water shortages, and other failures in city management.

Mumbai has evolved into the major domestic financial centre with all key financial services from banks to insurance headquartered in its Central Business District (CBD). In the efforts to position Mumbai as an international financial centre major reforms will be required in diverse areas concerning housing, transport and urban infrastructure. The reforms need to address the planning, regulation and financing of the city development.

This chapter covers the key measures that will have to be addressed to reduce the total quality adjusted cost of establishment in Mumbai in making it an attractive financial centre. The measures are

- Transport System Upgradation
- Urban Rehabilitation Project
- Decongestion of South Mumbai
- Upgrading Telecommunication Infrastructure
- Critical Reforms in the Real Estate Markets

2.2. Transport System Upgradation

The Issue

The transport problems of a city of 10 million people are complex. Mumbai's has had the ability to employ a large number of migrants, and to transport them over long distances through a relatively inexpensive and surprisingly efficient public transport system. But ironically, the relatively better infrastructure in the city is also resulting in the virtual collapse of the city and its infrastructure.

At present 88% of all travel in Mumbai is by bus and rail. Since the 50's, although passengers on the trains have increased five folds, the number of train trips have increased only 2.5 times. As a result, there are regular breakdowns.

Mumbai main problem has been an inability to raise adequate resources to improve existing public transport system. Both bus and train services are subsidised and fare collection cannot pay for their services leave alone expansion. In the 1970s, the World Bank was approached by the state government for funds to improve Mumbai's public transport system. This resulted in the first Mumbai Urban Transport Project (MUTP I) worth US$25 million which financed an additional 700 buses and fly-overs at three important road intersections. MUTP II (now renamed MUTP) is presently being negotiated and only recently has the last hurdle, the World Bank's condition that the railways set up a separate corporation for suburban railway services, been cleared. Subsequently, the Mumbai Railway Vikas Corporation, a joint venture between Indian Railways and the Maharashtra Government has recently been incorporated for implementation of MUTP.

Background

A few details of Mumbai's Public transport system are presented below.

- Load of trains = 4 times bus load in terms of passenger kms of travel
- The local trains carry 5.5 million passengers every day.
- Peak hour load = 4200 per train which is 2.5 times capacity
- On a typical day[5], WR operates 923 trains and CR 1072 trains

Solutions

Detailed exercises have been undertaken regarding integrated transport planing for Mumbai. The most recent of such studies have been a relevant study by WS Atkins conducted in 1994. Currently the Bombay First Transport Committee is also preparing a transport plan initiative, which focuses on a new integrated plan for the city.

[5] according to the Mumbai Metro Planning Group (MMPG) study

Given the magnitude of current and potential traffic, geographical layout, high density of population, Mumbai's transportation planning is a complicated problem in itself requiring co-ordination among efforts at:

1) further land use planning
2) decongestion operations (shifting of manufacturing operations to city fringes)
3) rail and road transport capacity overhauling

The objectives of comprehensive transport plan are:

- Integration of transportation with land use for mutually supportive systems
- Priority for appropriate investments in the mass transport systems
- Development of new modes with a minimum requirement for land, such as water transport
- Rationalisation of goods movement with regard to efficiency and competitiveness
- Transport services improvement in fringe areas of the MMR to improve inter-regional connectivity
- Integrated transport system development with appropriate interchange facilities

Further details of the recommendations are provided in the Annexure on transport systems.

2.3. Urban Rehabilitation

Issue

One half of Mumbai's population lives in slums and squatter settlements. This is primarily as result of affordability constraints owing to low incomes insufficient access to credit on the one hand the poor delivery system of housing.

The failure to create adequate low-income housing stock is one of the causes for aggravating problems of improvement of slums and maintenance and upkeep of existing housing stock. There is a severe shortage of houses in the city; only 20,000 houses are supplied against an annual demand of 70,000 flats.

Background

Mumbai's per capita income is 3 times higher than that of the Maharashtra State. However, despite this

- Over 3 million of Mumbai's residents live below the poverty line
- Over 50% if the population live in slums and informal settlements

Consequences

The associated problems arising from the unplanned growth of slums include

1) Deleterious effect on safety and hygiene
2) Pressures on urban infrastructure due to unplanned growth
3) Encroachments into lands reserved for infrastructure purposes.

Impact on land use patterns : The slums are located on land owned by the central and state governments, the municipal corporation, private individuals and lands belonging to the airport authority, the port authorities and the railways. Over time, as slums have begun to constitute important centres in various city, state and central electoral processes, most slums on state or private lands have now become permanent establishments and are provided basic amenities and are protected from demolitions. This does not allow development according to original land use plans.

Impact on transport systems : Settlements that have come up along the railway tracks are located just a few feet, often as close as three feet, away from the railway line. As a result, fast and superfast trains that run at peak hours have to slow down to a speed of 5 km/h when they pass these sections. These bottlenecks prevail at different points along the tracks, reducing the train turnaround time. Clearing up would result in improved speeds thereby freeing up capacity.

Solutions

The projects proposed under MUTP - II (now renamed MUTP) would involve a substantial number of households and structures to be relocated. Necessary resettlement and rehabilitation of project affected persons therefore, are as per the guidelines of the World Bank financed projects. The rehabilitation ad resettlement of the affected people would be an integral part of MUTP and MMRDA would be responsible for implementing the same.

Need for evolving a joint plan: There is a clear need for all the involved parties to work together to evolve a joint plan to solve the problem. In 1989, the enumeration of slum dwellers established that there were 18,000 households living along the tracks. In the last ten years, their number has grown to 25,000. The **State Government,** the **Indian Railways** and Multi-lateral agencies such as the **World Bank** will have key roles to play in evolving the rehabilitation project, facilitating and financing the same respectively. The relocation of these communities is critical in order to increase the speed of their trains, or to build additional lines.

Identification of alternative sites for relocation of slum dwellings : Temporary solutions such as withdrawal of settlement by a certain distance from their existing position near the tracks will not aid in the long term creation of transport capacity.

Resettlement of people to alternative locations with a more secure tenure in their new location needs to be thought through. This should also be accompanied by the clear demarcation of railway land to prevent resettlement on the rail property.

Assistance in establishing low cost housinq : The State Government will have to assist the slum dwellers in establishing low cost housing projects in the areas for relocation. Free housing or land may not constitute a solution to the problem as this could lead to demand from other project affected communities for the same which may not be possible to replicate.

The State Government can involve NGOs such as SPARC which have demonstrated significant success in undertaking the implementation of these projects. The projects can to a large extent be partly financed by the slum dwellers. They will also have to be supported by institutions / co-operatives that provide credit for housing needs.

2.4. Decongestion of South Mumbai

Issue

Closely associated with the transport problem is the fact that most financial services headquarters and other corporations are headquartered in South Mumbai. Financial services, both competitors and non-competitors, have exhibited a tendency to locate at close proximity to each other. While this is advantageous, improved telecommunications and rising costs can encourage firms to move out parts of their operations out of South Mumbai.

Consequences

Given the linear geography of the city, the concentration of offices in South Mumbai has resulted in

1) Very high real estate costs in select areas
2) Congestion of office space and parking
3) Unidirectional traffic at peak hours of the day leading to stress on road and rail transport infrastructure

However non-financial services companies have already begun movement out of the South Mumbai to other parts of the city on account of cost considerations.

Solutions

High workforce intensive financial operations to be incentivised to shift out : Many office such as ICICI, Citibank and UTI have already established state-of-the-art offices in complex as the real estate values here were significantly lower. Similarly more such organisation may be incentivised to shift. For example, large public sector corporations such as the PSU banks, LIC and GIC employ significant number of staff at the headquarters, involved in back and middle office operations. The shifting of these operations to alternative office could result in a win-win situation for all.

Developing additional centres as a counter magnet to South Mumbai : The MMRDA is in the process of developing an International Finance and Business Centre (IFBC) on an area of 130 hectare in the Bandra-Kurla Complex. The proposal aims at creating necessary facilities and supporting services to promote growth of international finance and business activities in Mumbai. The IFBC will include offices of the merchant bankers, foreign financial institutions, commercial banks, public sector financial institutions, regional head quarters of multi-national companies and other business houses, offices of the professionals and data base and computer software services. The new National Stock Exchange and the new Diamond Bourse being set up will form part of the proposed IFBC. To induce more organisations to establish operations in this area, the State Government / MMRDA needs to

- **Set up accompanying facilities** : A large ***International Convention Centre*** and a ***5-star hotel*** are absolutely critical in the alternate location. However on two occasions the institutions that bid for the hotel project have backed out. MMRDA has also indicated plans for other projects that need to be established urgently, such as

  - Educational Institutions
  - A Centre for Contemporary Culture
  - Multiplex Theatre and Entertainment Centre
  - Shopping centre, & Hotels
  - Underground car parks

  Housing facilities need to be segregated from the financial centre as the cost of developing high value infrastructure at the financial centre would be wasted on housing which can be developed on lower cost areas. However a provision for high value **housing** options for the top management of the corporates that will be based in the financial centre, should be provided for.

- **Enhance connectivity** : The MMRDA is planning a new rail link between Bandra and Kurla Railway Stations, providing direct access to the IFBC. In addition construction of access roads and storm water drains, sewerage and water distribution network is in progress.

- **Landscaping** : As the area surrounding the complex has consists of slums and marshland it is important that MMRDA invests in landscaping the entire area. An International Financial Centre cannot co-exist with poorly developed adjoining areas. This will be a deterrent in attracting potential international customers to the BKC. The two solutions for separating the IBFC from the adjoining areas include

  a) shifting of critical settlements in the areas to alternate locations (like the Shanghai Pudong Financial Centre)
  b) developing the fringes of the Complex with high rise buildings that effectively shield the rest of the complex from slum settlements. These complexes can be leased out at lower rates.

  c) Develop parks and recreational facilities : A **Mahim Nature Park** has been developed in conjunction with Worldwide Fund for Nature – India. More such parks and recreational areas need to be developed.

2.5. Telecommunications in Mumbai

The Issue

The main issues in any telecom network as in the case with the Mumbai region are threefold

- Quality of Service
- Quality of Customer care
- Cost of the services offered

The quality of any network is defined by the **uptime** of the line (world standards of 99.9%) and expansive bandwidth to meet the data transmission requirements. Other indicators of quality are the **fault rate**, which is 20 per 100 telephones per month in Mumbai (less than 2% abroad), and **mean time between failure** for an individual subscriber – which is five months for MTNL Mumbai as compared to four years for British Telecom, 5 years for telecom services in Japan and ten years for telecom services in USA. While the current in Mumbai are far improved as compared to earlier years, they still fall short of standard at a typical international financial centre.

Background

The Indian Telecom Industry has been state controlled since beginning and is in the process of being privatised lately (with introduction of private basic services operators, mobile telephony and ISPs, etc.). The state control on the telecom infrastructure, the monopoly status of the service providers and the third world status of the country has meant that there has been inadequate focus on development of a reliable and efficient telecom infrastructure and poor customer service. This has resulted in poor telecom density, outdated infrastructure, poor reliability and high downtime.

The quality of service in any network depends on the network technology. The network technology in Mumbai is outdated, especially the last mile connectivity part, connecting the telephone exchange to the customer's premises.

Consequences

Telecom infrastructure is the most important link between people around the world. Teleconnectivity is increasingly becoming the most important medium of trade, commerce and provision of service through out the world.

This is more so, in the case of a financial sector, where majority of transactions and trades happen on phone or through telecom related infrastructure and systems. Having a modern, reliable and efficient telecom infrastructure is very essential for any modern city with ambitions of becoming a financial centre. Thus, Mumbai's poor telecom infrastructure and services might be an impediment to the shifting of telecom dependent businesses especially with regional competitors like Singapore and Hong Kong having excellent telecom infrastructure.

Solutions

The Telecom infrastructure is Central subject with Department of Telecom being the nodal policy making body and service provider in most parts of India. The Government has started taking the right steps by increasing private participation in the telecom services and removing the monopoly status of service providers

The lccal network is managed by a Central Public Sector Undertaking which is a PSU operating a monopoly service provider in cities of Mumbai and Delhi.

Improving service quality : The main problem in improving the quality of service is the last mile connectivity, which is still through copper wires. MTNL is trying to tackle the problem by taking the exchanges closer to the customer or bringing the customer closer through superior links of fibre in local loop (FLL) and wireless in local loop (WLL) technology. The closer distance improves line reliability and reduces down time of individual lines. The use of FLL and WLL and Remote subscriber units (RSUs) also improves bandwidth availability for reliable and faster data transfer.

Setting up citywide broadband network in financial centre areas: Communication technology is undergoing rapid advancements that have aided businesses to scale up efficiencies. Internet and broadband access are one such development. The financial centre should have state-of-the-art internet connectivity will enable

a) high speed high capacity data transmission capabilities with other markets and development centres
b) enables services such as video-conferencing capabilities, e-commerce services, superfast internet access etc..

Reduction in cost of services : The cost of service issue would be addressed by the introduction of competition, which would lead to decline in cross subsidies, etc. MTNL's will now face competition from Hughes Ispat in providing basic services in Mumbai. In the mobile telephony segment, it will no longer remain the existing duopoly with MTNL's planned foray. In the ISP segment also new players are establishing operations. Competition will automatically improve cost of services, quality of services

Bombay First Telecom Committee has a proposal for establishing a Pilot Metropolitan Data Network for the financial sector in Mumbai. This will be a high speed network using optical fibres. It is planned to start a company to be known as " Financial Services Network (India) Pvt. Ltd." to implement the project.

2.6. Reforms In The Real Estate Markets

The Issue

Real estate in Mumbai is among the most expensive in the world. There is shortage of quality real estate properties both for business and residential purposes at affordable prices. The property price variation in different parts of Mumbai is very high and so is the price volatility of real estate markets, which could make investors nervous. The problem is linked to the two legislations, a) the Mumbai Rent Control Act and b) the Urban Land Ceiling and Regulation Act.

Background

The Mumbai Rent Control Act affects nearly 80 per cent of the population of the metro. The Act, which came into force in February 1948, has always been a bone of contention between the tenants and the landlords. It was initially meant to be only for 5 years to protect tenants against evictions and demands of high rent, and has since then been extended periodically.

- As per the Act, the standard rent, i.e. the maximum legally permissible rent a landlord can collect, was pegged as the rent as on September 1, 1940. For buildings constructed later, the standard rent was the first rent paid, when the property was let out. This had been treated as grossly unfair by the landlords.
- The Supreme Court directed the state government to legislate fresh provisions that would be equitable to both landlords and tenants. Tembe Committee report (1975) contended that the rent-freeze had worsened the housing problem in the city.
- Maharashtra Law Commission (1979) contended that increase in rents should be allowed, as 75 % of the landlords were middle class persons relying on rent payments for livelihood.
- Model rent control legislation (1992) called for a balanced approach towards the landlord and the tenant. The landlords are all for it as it provides for increasing the rent to market levels within five years.
- The state government has subsequently, passed an amendment bill. The bill allows for a 4% annual increase in standard rent and has also legalised the pugree system.

Consequences

- Legislations such as rent control and the ULCRA distort the real estate market which is a capital asset, by artificially distorting the demand supply balance of housing stock and other real estate. Moreover these acts impede the development of Mumbai.
- Housing units locked up in preference to being rented out. Rationalisation of rents would open up many of these flats and ease the housing problem in the city. Deposit is an advance paid by the tenant to take a flat on lease. This came to being as a consequence of the frozen rents and a shortage of fresh housing.
- The current systems are known to create a high volatility in the real estate market prices. Given that many bank loans are secured by real estate assets, volatility in the prices could have a negative impact on the banking systems also.

Solutions

- Rent control is highly sensitive issue, which the state government is attempting to resolve. The issue will need a consensus on from various interest groups. The State government needs to keep in mind that land reforms are critical, while the implementation process may be phased out in a manner that will minimise impact on parties. Phasing out the Rent Control Act will also mean phasing out the pugree (a non-returnable deposit), where prospective tenants pay high advances to take houses on rent. However tenants who have paid a high pugree will stand to lose. Phased repeal may imply that property rented after a particular date should not be under the purview of the Rent Control Act.

- The new rent control act, allowing 4% increase in rent annually and legalising the system of "Pugree" has been passed and has received Presidential assent. However, the efficacy of the new rent act, to free up housing for rent remains to be seen.
- In addition the phasing out the Urban Land Ceiling Regulation Act (ULCRA) will release large tracts of undeveloped land belonging to the different bodies of the state government such as Mumbai Port Trust, CIDCO, National Textile Corporation and the Railways and Indian Navy. Over 6,000 acres are estimated to be locked. In the middle of Mumbai, 180 hectares of prime land belonging to 58 non-functioning mills, forbidden by law, lie unutilised. Some of the mill properties, however, are in the process of being developed. Even if a portion of this is released, prices could be brought down making property more affordable.

- Another interim solution is the movement of offices, especially the mid-office and back-offices of various financial services, to lower cost locations like Bandra-Kurla complex, Andheri and Belapur. As per the Colliers Jardine report. The rentals at Nariman point are in the range of Rs 125-165/sq ft/ month as compared to Rs 70-90/sq ft/month in Bandra-Kurla complex and Rs 40-60/sq/ft/month at in Andheri area.

3. Comprehensive Transport Strategy for Mumbai

3.1. INTRODUCTION

The function of a city's transportation system is to provide for the movement of people and goods. The Gateway of India was once a paradise of beautiful buildings with a streamlined and efficient transportation system, which included the country's only suburban railway service. But Mumbai today shows all the signs of urban decay.

In the past, various transport studies have been carried out by different consultants over the years. Many of them have remained on paper and no priorities have been established.

Bombay First Transport Committee has undertaken to prepare a Comprehensive Transport Strategy document for Mumbai City. This would be on the lines of a document prepared by the London First Transport Initiative entitled "London's Action Programme for Transport: 1996-2010". This document will form the basis for advocating a holistic transport plan for the city. Such a document would cover the following:

It will prioritize the various transport projects over the next ten year period.
Design a methodology and recommend long, medium and short term measures for the development of rail, road and water transport.
Address issues such as parking, alternative traffic corridors, area traffic control systems, etc.

While preparing this document, the focus will be on upgrading public transport, taking measures to improve its effectiveness and expanding its scope, to copy with the increasing population in the city. The draft document will be discussed with different government agencies before it is finalised and published. It will be widely circulated to the Government and to the corporate sector.

3.2. BACKGROUND

Mumbai's Public Transport infrastructure has not been able to cope with the growth of population and economic activity and because of lack of investments in public transport there are tremendous hardships to the commuters and delays and uncertainties in reaching their destination.

The population of Mumbai Metropolitan Region (MMR) which was 14.4 million in 1991 is expected to increase to 22 million in the year 2011. Formal sector employment in the city region was 3.8 million in 1993 and expected to increase to about 5.3 million by the year 2011. Informal sector employment will account for about 30% of the total.

Consequent to increase in disposable incomes, private vehicle population in the city is expected to increase from 6,35,000 in 1991 to over 2 million in the year 2011.

However, the city of Mumbai has an organic street pattern that is fixed, with very little possibility of change. The area under roads is barely 8% while other cities of like magnitude have about 25% of their area under roads.

Overall travel demand will grow by approximately 51% in line with population growth and rising incomes. In 1991 about 88% of peak hour journeys were made by public transport and this proportion is expected to remain high at between 85% to 86% in the future resulting in 47% increase in peak public transport demand. Unfortunately, increase in the capacity in case of both suburban railways and buses has remained more or less stagnant resulting in tremendous pressures on the suburban railway system and the BEST, thereby encouraging higher private vehicular traffic.

Mumbai's rail based mass transportation was the best in the country. Trains ran on time, and people arrive in good shape. Productivity was high. Today, the Mumbaikar wages a daily battle to get to his office, and then wages another one in the evening to get back home. In between, he tries to put in some work. There are a large number of households in Mumbai where the children meet the man of the house only on the weekend, because he leaves home before they are up, and gets in after they are in bed. Today, Mumbai's trains carry over 4500 persons, as against the actual capacity of 1800 persons. This is 50% higher than the trains of Tokyo, which are considered to be the most crowded in the world.

3.3. COMPREHENSIVE TRANSPORT PLAN FOR BMR - W.S. ATKINS REPORT, 1994

At the behest of World Bank, M/s. W.S. Atkins - U.K. has in their report of 1994 recommended a comprehensive transport strategy for the Mumbai Metropolitan Region (MMR) and the investment plan was prepared for the period 1995 - 2011. The bulk of the programme was for development of railways (72%), highway schemes (21%) and bus and ferry systems (7%). The project for the two 5 year phases - Phase - I (1995 to 2001) and Phase-II (2001 to 2006) as under :

	Part	Total Number Of Projects	Cost at 1992-93 Prices. Rs. in Cr.	Total cost in %
A.	Metropolitan Railway System Development	20	5,300	72%
B	Bus and Ferry System Development	Bus-3 Ferry-3	567	07%
C	Highway Scheme	39	1,522	21%
	TOTAL	65	7,389	100%

In addition, the plan did identify some long term rail and road investments which included the Mumbai Trans Harbour Link (both by road and rail), the Worli-Bandra bridge and Western Island Expressway programme to be undertaken at the end of the "core" programme worth Rs.7,389 Crores, and dependent on additional funding becoming available.

Priority was to be given to the railway system at this was considered to be the optimum feasible means of serving the bulk of the future transport needs of MMR and catering to the projected 47% increase int he peak public transport demands. Besides, the railway connection from Kurla to New Bombay and 3 East-West rail links were proposed.

3.4. TRAFFIC IMPROVEMENT MEASURES:

The Atkins Report has laid considerable stress on improving the existing link roads and increase in network capacity such as :

- Connecting of Mahim road overbridge over the Western Railway to Senapati Bapat Marg by a ramp.
- Construction of a fly-over to carry the Senapati Bapat Marg to Dadar (West). This has been completed.

The Report has also laid considerable emphasis on optimising the existing main road network by more efficient use of the Right Of Way (ROW), the control of parking, junction improvement through traffic management measures for most part and traffic control systems. The major feasible investments designed to promote the efficient use of the existing street system in Mumbai city are intersection redesign, one way traffic systems, traffic signaling and provision of bus lanes.

Pedestrians

Pedestrian movements are very high throughout the city especially near railway termini, in main business / shopping centres, and on the approaches to the railway stations.

Footpaths are too narrow or are encroached by hawkers, where as in the suburbs they are often non-existent. Where there are footpaths, they are frequently poorly maintained through excavation and inadequate reinstatement by the utility companies. As a result, many pedestrians have to perforce walk on the carriageway with consequent safety hazards as well as loss of traffic capacity. This coupled with parked vehicles, etc. results in the limited available right of way in many areas not being optimally utilised. Removal of encroachments from footpaths would encourage pedestrianisation thereby reducing considerably short vehicular trips in crowded city centres and releasing precious roadway capacity.

Parking

Due to inadequate onstreet parking lots available, many roads are fully parked during business hours and double-banked parking, particularly by taxis, is not uncommon especially in Fort area. This further reduces the capacity of the carriageways. Municipal Corporation has recently introduced pay and park schemes. This needs to be extended and more incentives have to be given for multi-storeyed parking particularly in the island city. Strict control on unauthorised parking, even on taxis, is essential.

Optimising Existing Road / Network

There is a strong movement in the North-South director for work, and this loads all the existing corridors in this direction, beyond their capacity. At present, in the road network, there is only the Western Corridor along Lala Lajpat Rai Marg, the Central Corridor along Dr. Ambedkar Marg, and to some extent the Eastern Corridor along P.D'Mello Road,

An analysis of the street system of Mumbai will show that there are several possible road corridors that can be upgraded to arterial roads to handle this tidal flow of traffic, instead of constructing new corridors. One of these is Senapati Bapat Marg, which is a road corridor that runs right through the centre of the island. This is a 6-lane roadway which is heavily encroached by slum dwellers, unauthorised garages and idle parking. The road passes through the mills area of Mumbai, and so has a very blighted look. This road should be cleared of encroachments, and the slum dwellers should be rehabilitated. Parking needs to be organised, and priced. Road geometric needs attention, along with road signs and markings. Two new fly-overs are under construction on this road.

It has been stressed in all transport studies done in the past that first priority should be to take other measures to utilise the wide interior roads which are presently underutilised viz. Khan Abdul Gaffar Khan Road and Senapati Bapat Marg between Mahalaxmi and Mahim. There is a proposal to extend Senapati Bapat Marg from its dead end at Mahim towards Bandra at Carter Road junction by providing a bridge near Mahim creek and subway below the expressway with suitable connecting embankment. This would enable part of the traffic from the north to be diverted on to Senapati Bapat Marg thus reducing the load at Mahim.

Similarly, the Eastern Corridor also needs to be upgraded, although the roadway parameters are all in place on this corridor. Here the road signage and environmental aspects need to be taken care of alongwith clearing of slum dwellers and encroachments. Traffic needs to be encouraged to use this corridor, instead of the Western and Central Corridors.

This will create four strong, North-South Corridors, in addition to the five rail corridors.

East West connectivity is poor as at present, and this needs to be augmented, in order to reduce the loads on the few links that provide access in this direction. Again, a study of the road network reveals several possible road links existing, that can be upgraded with minimal cost, to improve the East-West connectivity.

Mass Transportation

The use of mass transportation needs to be encouraged by all sections of the society, by giving a deterrent of some sort to the use of private transport, while at the same time improving the quality of the mass transportation services. This deterrent may be in the form of cordon pricing, or minimum car occupancy required to enter a particular zone, or heavy parking charges.

Bus services should be redesigned to provide a feeder service from the railway stations / water transport terminals to be peripheral areas. More air conditioned buses on long routes also should be introduced, so that more private car trips are shifted onto the buses, and road congestion is relieved.

3.5. RAILWAYS - MUTP II

The railway should be augmented to provide a much higher level of service, so that these become the main corridors of travel in the North South direction. Air conditioned coaches also should be added to the railway system, to draw the upper classes away from their private cars to mass transportation.

Based on the W.S. Atkins committee reports, Mumbai Urban Transport Project (MUTP) II was taken up and priorities for rail and road projects have been established. The world Bank mission during its last visit has finalised this programme and it is expected that a World Bank loan will be sanctioned which includes rail components of Rs. 3,063 crores. It is expected that at the end of the first phase spread over a 5 year period, the peak hour capacity of the suburban railway system will increase by 25% on the Western railway and 27% on the Central railway. The road component of the project covered mainly the areas like BEST bus procurement, area traffic control system, traffic management programmes and some rail over bridges.

The World Bank mission has raised serious concerns about the ambitious fly-over programme of MSRDC without apparent public consultation and environment & traffic assessment. The Maharashtra Government advised the World Bank that construction of new fly-overs in the island city will be stayed till a study is completed and discussed with World Bank.

3.6. WATER TRANSPORT

It is possible to utilise Mumbai's natural resources of water to provide Passenger Water Transportation along the coastal routes, especially along the East Coast, and between Mumbai and New Mumbai. There are a lot of small jetties and wharfs existing at Mazagaon Dock, New Ferry Wharf and Pir Pau that can be upgraded at low cost to handle the Passenger Water Transportation traffic. This route is also a sheltered one, unlike the West Coast route, which is exposed to the tides and the monsoon, and can e operated all year round.

3.7. PROPOSED PROJECTS

Mumbai Trans Harbour Link (MTHL)

The Mumbai trans Harbour Link is proposed as Road-cum-Rail link from the Island of Bombay to the mainland to improve accessibility to the mainland. The Link is proposed to take off from Sewri on the Island and meet the mainland at Nhava. Interchanges are proposed at both ends of the bridge. At Nhava, the link will connect with the Panvel-Belapur Road and with the NH17 to Pune. The length of the Modified Alignment for Road Link is 22.85 km. And the Rail Link is 20.40 km.

Bandra-Worli-Nariman Point Sea Link Project

This link is proposed to improve accessibility to South Bombay. The Link will take off from Mahim, connecting with the Western Expressway and go south along the coastline upto Worli where it will provide a take-off point with an interchange connecting it to Dr. Annie Besant Road. The current connection is at Worli Sea Face, but an alternative has been suggested at the Drainage Channel Road, and this is being considered.

From Worli, the Sea Link will continue through the sea to Nariman Point, with two connections to the island at Haji Ali and Priyadarshini Park on Napean Sea Road, before it loops around Raj Bhavan, and proceeds towards Nariman point. From Nariman Point, there is a spur across water connecting to Cuffe Parade also.

The Sea Link is expected to provide much needed relief to the road users on the 3 corridors of the island.

Eastern Freeway

The construction of the MTHL would result in a traffic diversion from the present Thana Creek Bridge onto MTHL. This will bring the traffic directly onto Acharya Donde Marge and other internal roads of the island. If a proper dispersal system is not put into pace simultaneously result will be utter chaos and congestion on the island. The Eastern Freeway would therefore be necessary to disperse the traffic to the North and South of Sewri.

The proposed alignment of the Eastern Freeway from Museum to Sewri goes over Mumbai Port Trust property. It is hoped that Mumbai Port Trust will provide the necessary right of way through their lands for the Freeway.

Anik-Panjrapole Link Road

This road will provide a vital connection in the eastern sector by passing the congested are Chembur.

Bandra-Kurla Rail Link

The existing suburban railway system runs in the north-south direction and the only point of integration is at Dadar. This loads the system upto Dadar excessively and commuters wishing to move in the east-west direction are forced to add substantially to their time and cost by going upto Dadar to change over.

The entire pattern can be changed if the Bandra-Kurla Rail Link is provided. This will provide accessibility to the Bandra-Kurla complex also. This Link was originally part of MUTP but has been deferred.

Light Rail Transit

The implementation of the Light Rail Transit project in the CBD and the suburbs of Mumbai need to be accelerated. This will improve the mass transport connectivity from the two suburban railway stations of Churchgate and CST to Nariman Point and Cuffe Parade, both of which are huge generators of commuter traffic. The suburban link will improve accessibility to the international airport at Sahar. If this is in place, the number of buses can be reduced, leading to substantial decongestion of surface road space. These buses can de diverted to other parts of Mumbai where augmentation of bus services is required. This will also cause a substantial reduction in the requirement of shared taxis, and taxis, which are currently a major cause of congestion on Mumbai's streets.

3.8. MUMBAI METRO NETWORK – 7TH CORRIDOR

To solve Mumbai's transport problem on a long-term basis, a proposal for Mumbai Metro Network underground railway has been submitted by Tata Consultancy Services in 1997. A detailed pre-feasibility study for constructing and operation a 7th corridor in Mumbai, as proposed by the Indian Railways about 25 years ago was undertaken by a consortium led by TCS. This study was completed by December 1997 and a report submitted to all concerned. The financial model for the scheme assumes that the government would only be a facilitator and most of the funds would be raised through private participation.

3.9. CONCLUSIONS

It is obvious that Mumbai's transport system has suffered not because of resource constraints but because of wrong priorities being given like private transport vis-à-vis public and road vis-a-vis rail.

What Mumbai needs is an integrated transportation system, with the rail based mass transportation services providing the core of the system, and road-based mass transportation including Light Rail transit providing a supplementary rather than a competitive services. This means that the points of integration between the various types of modes need to be addressed, with the objective of streamlining the transfer from one mode to the other. These Inter-Modal transfer points are crucial to the success of the integrated transportation system. If this can be achieved, then Mumbai does not any additional traffic corridors in the immediate future, air pollution levels can be expected to drop, stress parameters can be reduced or eliminated, and total journey times can be reduced. Mumbai will once again have a transportation system that works.

Comprehensive Transport Strategy for Mumbai - prepared by Bombay First Transport Committee.

4. MUMBAI AS AN OFC :

4.1. The potential of Mumbai to become an OFC

- Mumbai's historic development as a national financial centre has bee due to:
  - High quality entrepreneurship.
  - Skilled workforce.
  - Safe port facilities.
  - Efficient & "user friendly" administration
- Country's leading and established financial centre for over a century, but catering largely to domestic financial markets.
- Advantages over other financial centres in the country such as Chennai, Calcutta, Delhi or Ahmedabad, in terms of size, depth and efficiency.
- Presence of head-offices of leading national financial institutions and commercial banks.
- Established capital markets contributing to nearly 75% of total market capitalisation.
- Presence of large number of firms providing related services, such as brokerage, accountancy and legal.
- Availability of skilled labour which can learn quickly, including good IT support.
- Attractive intermediate time zone.
- User of external funds will be compelled to look for other options for meeting their massive and complex requirements of finance in other off-shore centres.
- Instead of net growth in employment and income from financial services, we will see a steady decline.

The loser will not only be India, but more importantly, Mumbai itself - no substitute for decline of manufacturing.

4.2. Benefits to Mumbai

- Direct job creation in front offices - highly skill oriented.
- Creation of a range of service jobs requiring different skills at different levels.
- Experiences elsewhere has shown that such financial centres also create jobs in the hinterland of cities as back-offices and ancillary support services move out of the financial district.
- Increased City revenues
- Designated authority to operate facilities within the financial district.
  - * Stiff user fee to be charged by the State/Municipal authorities.

* Funds generated by this can be used in other important city projects, viz., improving urban transport, solid waste management and providing low cost housing.

- The overall benefits of creating a Regional (and subsequently international) financial centre at Mumbai would greatly outweigh the one time costs of creating the necessary infrastructure.
- Mumbai has an important role in this transition to a financial centre. Incremental costs of infrastructure must consequently be borne proportionately by GOI also.

4.3. Location

In terms of location, Mumbai, like many OFCs, is an island. It is situated in such a time zone as to form an ideal link between the offshore centres of Singapore and Bahrain. It can provide simultaneous links with Asia, mainland Europe and London with the time gaps being four to five hours on either side. Mumbai is the financial capital of India and has financial expertise available from both the Indian and the international banking sectors, as well as other financial sectors. Mumbai is also home to several international accountancy firms, consultancy firms, and reputed legal firms.

The agglomeration economies, i.e. the external economies of scale between firms, is an important reason, why Mumbai, should be preferred as an Offshore Centre for India. Many of the Head Offices and forex and money market dealing centres are situated in Mumbai. This can allow for the updating of knowledge, innovation and cross-fertilisation of ideas, which can be capitalised for starting an Offshore Centre. Like London has made the best use of those kind of natural advantages, to have the biggest international financial centre in the world, we can make use of Mumbai's agglomeration of financial economies of scale to start an offshore centre. In this context, it is relevant to quote the finding of a research study, sponsored by Bombay First, done by Prof. Lalit Deshpande, former head of the Mumbai University Department of Economics and Dr. N Hatekar, faculty member of the same university (D and H study). The aforementioned study has reported that the employee efficiency was high in Mumbai and the important reason for the relatively high efficiency of Mumbai is the high density of the formal and informal financial firms in Mumbai. According to D and H study the informal sector provides to the formal sector a low cost highly skilled network of brokers, agents and sub-agents. The early access to this network creates increasing returns to location in Mumbai.

Another factor that has influenced the successful functioning of an offshore centres is the location of the centre timezone-wise. India is definitely at an advantage as it is between London and Singapore. We are five-and-a-half hours in advance of London ad two hours behind Singapore. We can transact on the same day with London and Singapore. Bahrain is the only centre which enjoys timezone-wise. Any proposed offshore banking facility in India would really be a bridge between the Asian and Euro-dollar market. Bombay with its tradition of banking and trade would be an ideal choice for locating the proposed OFC.

The current development trends of Mumbai are that the industry and physical markets are moving out into the mainland and Mumbai is increasingly becoming an administrative and financial hub. Mumbai therefore appears to be an ideal location for an OFC if one were to be initiated in India.

4.4. Technology

While Mumbai does not have a telecommunications network of world class, it is fast catching up and today's shortages and malfunctions will soon be things of the past. As far as technological competence is concerned, India has the much talked-about pool of technical labour in all fields in abundant quantities. The computing facilities in Mumbai, in terms of requirements of both men and machines may not be found wanting.

4.5. Infrastructure

The infrastructure in Mumbai suffers from several deficiencies, typical of agglomeration diseconomies. First, land and office space is one of the most expensive in the world. The archaic rent laws make it difficult to lease office space. The same is applicable to housing of the non-resident staff that would be posted should Mumbai be declared an OFC.

Mumbai, a megalopolis, is home to 10 million people. The transport infrastructure, disproportionately dependent as it is on the hundred-year-old railway system, is on the verge of a complete breakdown. The roads are inadequate and there is a very high density of vehicular traffic leading to legendary bottlenecks.

However, Mumbai is well connected to all major centres of the world by air. Further it is also well connected and at a reasonable distance from the vast Indian hinterland which is where the funds are likely to be deployed.

The labour laws in India put an onerous burden on an employer. The situation is particularly irksome in the areas of exit from the activity and retrenchment of unionised labour. The wages in Mumbai are also relatively high. However the positive side to the labour related issues is that there is easy availability of English speaking labour with a wide range of skills. The work ethic of Mumbai labour is better than in most parts of India.

The social infrastructure has its limitations due to scarcity of clubs, schools, and eateries of international standards.

4.6. Role of Bandra-Kurla Complex

Bandra-Kurla complex is not being created only to house offshore financial centres (OFCs) as its major focus. In fact it will house mainly new institutions like NSE, futures/options exchange, new commercial banks, insurance Companies, Fund Managers, Accountants, Solicitors, etc., as an adjunct to Nariman Point. What, then, will the city of tomorrow look like when it is no longer an `office city'? It will, one can safely say, be a `Headquarters City'. Twenty-five years ago, a number of large US companies – General Foods, IBM, General Electric – moved out of Manhattan and into suburbia, lock, stock and barrel. At that time, we did not know that we could move information. Thus, to free office workers from the need to commute, companies isolated top management people and professionals and imposed on them constant travelling into the city for business meetings. Big companies tomorrow are almost certain to keep their management people – at least their senior ones – where other senior management people are : in the city. And so will government agencies and other large organisations. But this means that the big city will also house purveyors of specialised skills and knowledge – the Lawyer, the Accounting Firm, the Architect, the Consultant, the Advertising Agency, the investment banker, the financial analyst and so on. But even these people will have their office work done outside the city.

4.7. Regulation

The Indian legal system is based on Anglo-Saxon jurisprudence which is widely accepted in the international financial world and the fact that there is very large English speaking population, with the superior courts functioning in English is a distinct advantage. However, the legal administration leaves much to be desired and disputes remain unresolved for unacceptably long periods of time due to the backlog of cases in all courts. The debt recovery tribunals specially set up to take up cases relating to the financial sector are suffering the same fate with added woes of challenges as to their constitutional validity. Other issues relating to proliferation of stamp duties need to be also considered.

There is a regulatory framework in place for the banking, non bank finance companies, the money and forex markets, the debt and equity markets, in short for the financial sector. There is also a codified legal framework for trust laws, company law, patent and copyright laws and accepted accounting standards. However, it is also true that major modifications will have to be made to the existing framework to bring it in alignment with prevailing international practices and standards. This, however, does not seem to be an insurmountable difficulty.

4.8. Political situation

India is a large functional democracy. At the present time there is fragmentation of peoples mandate and there is no political party which can be said to have the numerical strength to push through parliament any agenda which does not have broad acceptability cutting across political and economic ideology. There could be serious reservations from certain sections to opening up an OFC, related primarily to the twin fears of capital flight and tax evasion by residents. Tax compliance culture is conspicuously absent and capital flight in the face of rigid exchange controls and high rates of taxation is a fact, the tendency towards which remains.

The arguments will need to be studied very carefully in the light of our poor tax compliance culture. The various estimates on the extent of parallel economy run as high as 100%. Further, in spite of tight foreign exchange controls and a draconian law to aid implementation thereof, the estimates of flight capital are astounding figures. A large proportion of capital flight is attributed to use of the trade route in spite of having extensive machinery to check and assess valuation of all international trade.

The current tax structure and the collection machinery in India, both direct and indirect, although streamlined to a great extent, is still in the process of reform. The same is true for exchange controls, which have been liberalised to the extent of current account convertibility. Confidence in the continuity of reform process will perhaps reverse the trend in capital flight and in the habits of tax evasion.

One more politically sensitive issue relates to the possibility of crowding out of the public sector banks which dominate the banking sector. The public sector banks are heavily burdened with poor profitability, high levels of NPAs, high levels of operational expenses, excess staff, poor and inadequate levels of mechanisation, militant trade unions, non-discriminating system of rewards and punishment, inadequate numbers of staff trained in the modern products and their risk management techniques, low morale. The public sector banks are also charged with the responsibility of fulfilling the social upliftment agenda of the government.

The few people with the requisite skills are already the subjects of poaching and the trend would be significantly enhanced.

Since the socio-political environment will not permit a total revamp so as to exclude all protection to labour, a thorough relook at the Rent Control Act or remove the social obligations on the banking sector, one solution could be to follow the example of Singapore where the offshore banking licence permits only a limited activity in the local currency balance sheet. The limitation is imposed by way of restriction in the size of the local currency balance sheet.

The licensing norms will have to be carefully laid down for banks as well as non bank finance corporations. Internationally the BCCI debacle remains fresh in memory. Perhaps we may need to emulate Singapore in matters of licensing and regulation. There the licensing norms are strictly followed and it is reported that no interference from any quarter is tolerated. It is also reported that BCCI had tried various methods for getting a licence to operate in Singapore but the Monetary Authority of Singapore (MAS) had consistently refused to permit setting up shop. The MAS as a matter of routine examine the antecedents of all Bank chief executives posted in Singapore and expect the executives to monitor the activities of the forex and money market dealers to ensure compliance with local rules along with internal guidelines. The MAS take the audit reports and the auditors very seriously and have not hesitated to remove statutory auditors where they thought such action was called for. Basically, the MAS have consistently conveyed to the offshore players that the regulations were to be observed at all times by all and that any breach would be dealt with in accordance with laid down rules. The MAS's consistent and evenhanded application of the rulebook has given Singapore the clean image that is so necessary in the financial world.

4.9. Revenue and income generation

The licence fees, registration fees, stamp duties, corporate taxes are a substantial source of income in small countries. However, in a large country like India, it will not form a significant part of GDP. The more important aspect is perhaps employment generation and skills upgradation that is bound to take place.

4.10. Financial market development

Ever since the reforms were introduced, consistent efforts have been made to improve the financial markets. The establishment of an OFC will enhance these efforts by increasing the number of players and deepening the markets.

4.11. Other benefits

Allied activities like legal and accounting services, telecoms, transport construction, office equipment, hotels etc would all develop creating a better infrastructure.

McKinsey and Company, in their report (April, 1993) on Maharashtra writes, "Bombay's options in building a stronger regional presence and competing with Singapore and Hong Kong are constrained by several issues which characterize the current Indian financial services sector - capital market instruments such as debentures and warrants are thinly traded; advanced derivatives such as options and futures are yet to develop; money market instrument trading volumes are far below international level; market liquidity is low, with less than 10% of all listed scrips trading regularly on a daily basis; equity settlement times - 15 days - are much longer than developed markets due to low automation and complex legal and regulatory procedures; availability of timely, high-quality market information and investor protection trails international expectations; foreign investment climate still trails competing emerging markets in ease of entry, repatriation of income and associated taxes. Finally trading procedures lack automation, lack adequate transparency, and are perceived to contain uncurbed speculation and insider trading.

While these issues are largely beyond the control of the State government, have been studied extensively, and are being currently addressed, there are several attributes which support Bombay's continued development as a leading finance centre which the State could execute against. To prepare for the potentially imminent future entry of foreign financial institutions, Bombay should initiate a detailed plan to build an integrated finance centre complex with state-of-the-art telecommunications infrastructure, space for international financial services company offices and supporting professional services such as legal, computing and real estate, and an advanced banking institute to supply finance specialists. The proposed Bandra-Kurla complex could provide a sound option provided it is designed comprehensively with full supporting facilities and infrastructure. To support the centre, the city will have to increase the availability of high-quality residential accommodation for expatriates and high-income banking professionals.

To develop this concept, Maharashtra should initiate discussions with influential decision-makers (in particular, well-placed Indians) within leading international institutions such as Goldman Sachs, Morgan Stanley, Nomura Securities and Merrill Lynch to better understand their future expansion plans and needs, and develop a proactive marketing campaign promoting Bombay as India's Hong Kong (gateway to large domestic market).

Separately, the State should work with the BSE and NSE to evaluate the feasibility of setting up a futures and options exchange, increase automation to lower transaction costs and expedite settlements, improve market transparency, and reduce stamp duties to levels comparable with other states."

4.12. Conclusions

Capital account convertibility, perhaps, cannot be implemented fully in India at the present juncture. But offshore banking can be implemented in India, and preferably in

Mumbai, to take advantage of some more positive aspects of capital account convertibility. Here also, we may have to make some choices: it would be difficult to go for a tax heaven like Cayman Islands, Jersey etc, but an active offshore like Malaysia's Labuan model may be more appropriate, where a lot of free banking is provided basically to non-residents. Banking with residents and in domestic currency is permitted in limited ways only. However, some integration with domestic markets, through interbank markets, is also welcome, as then only the benefits of foreign inflows can be fully derived. But, how far the domestic currency book should be incorporated and enlarged is also a matter of policy choice.

Agglomeration economies make Mumbai the ideal centre for an OFC. Mumbai, already, has good talents in banking and offshore centre will further attract and develop it. Now telecommunication and infrastructure facilities are now developed, but they have to be developed further. Offshore financial centre employees should be able to use international airports with ease through green channels of customs check-up airports etc; Many of the legislative measures will have to be undertaken such as: change in income tax laws and withholding taxes, all Cash Reserve Ratios including basic three percent has to be removed in offshore centres, and full freedom on interest rate front has to be given. Other trusts, insurance companies, with more freedom and flexibility, will have to be provided at Mumbai offshore centre. Mumbai can become an offshore centre specialising in securities trading for non-residents. In the context of OFCs, non-residents can also include foreigners and foreign entities.

It also involves a high expertise on supervisory talents to avoid money laundering, etc., Mumbai will also fit into time-zone appropriate criteria to link various markets in the world. India is definitely at an advantage as its is between London and Singapore. We are five-and-a-half hours in advance of London and two hours behind Singapore. We can transact on the same day with London and Singapore. Bahrain is the only centre which enjoys such a favourable location timezone-wise. Any proposed offshore banking facility in India would really be a bridge between the Asian and Euro-dollar market. Mumbai with its tradition of banking and trade would be an ideal choice for locating the proposed OFC.

Mumbai has very distinct possibilities for developing into a global financial centre along the lines of London, though perhaps on a smaller scale. As a beginning towards achieving a global centre status, it would be good idea to convert Mumbai into an offshore centre with restrictions on the size of the domestic currency balance sheet. This would not create any undue pressure on the domestic financial system before it is ready to handle it.

It would create an opportunity for international capital looking for safe investment avenues simultaneously catering to the financial needs of India. The following estimates of footloose capital in search of opportunities for investment and the capital needs of India in the infrastructure sector alone are illustrative of the feasibility from the point of view flow of funds.

A 1996 survey of HNWI assets indicates the same at levels of USD 16.6 Trillion. Of these, the non-resident Indians (NRIs) had the combined gross assets at USD 300 billion and net assets at USD 40-60 billion. NRIs comprise some 15-20 million individuals and include a wide range of professional and business interests spread out across USA, UK, Middle East and South East Asia, and Africa. India's liberalisation programme is creating financial opportunities and encouraging a shift in focus towards India. A case in point is China. When investment opportunities were opened up in China, the overseas Chinese are reported to have invested half the total foreign investment in various projects.

A survey of funds with US pension funds reveals that they have USD 7000 billion for investment and the figure is estimated to go up to USD 12000 billion by the year 2000.

The opportunities for end use of funds are vast, as India is a large country in need of infrastructure of all kinds. The Rakesh Mohan Committee has estimated the investment need of the infrastructure segment at Rs 4000 to 4500 Billion (USD 115 to 130 billion) over the period 1996-2001. Over the period 2001-02 to 2005-06 the amount is estimated at Rs 7500 billion or USD 215 billion. The report further mentions that we could reasonably expect about 15% of the total capital requirements to be externally financed.

The Indian industry, long subjected to the Governmental controls by way of licence and capacity dictates, along with constraints on import of technology is in urgent need of modernisation and therefore commercial banking activities have a good scope and the corporates need not travel to financial centres for negotiations.

This step, however, needs to be taken with caution and only after going through the necessary legislative measures to make it possible to do business, not only from the point of returns, but also the ease of operations and a clean business environment. It would be necessary to ensure that funds rejected elsewhere are not permitted entry and the image sullied. A suitable Money Laundering Bill will have to be passed and it is advisable to incorporate the conditions adopted by the FATF which are be uniformly adapted in the EU. [Money Laundering Bill is already introduced in the Parliament of India.] The following table is a good guide to some key elements applicable in leading financial centres.

Our reputation for inordinate delays in completion of simple or routine tasks and the need to pay bribes at all levels will also have to be dealt with firmly and finally if the corporates and trusts are to be attracted in significant numbers.

Capital flight issues have plugged the country for long and this could be a way of attracting it back. Confidence of the international community in the continuity of reform oriented government policies will therefore have to be built up to ensure success of the OFC in Mumbai.

Many of the legislative measures now in progress in India including the Money Laundering Bill, can facilitate the starting of OFC in India at Mumbai.

Adapted from Offshore Financial Centre in India at Mumbai, A Report by National Institute of Bank Management

Laundry list - "High Priority" Laundering centres, March 1997

	A	B	C	D
Aruba	✓	X	X	✓
Canada	✓	✓	✓	✓
Cayman Islands	✓	✓	X	✓
Colombia	✓	X	X	✓
Cyprus	✓	NA	✓	✓
Germany	✓	X	X	✓
Hongkong	✓	✓	X	✓
Italy	✓	✓	✓	✓
Mexico	✓		✓	✓
Netherlands	✓	✓	✓	✓
Netherlands Antilles	✓	X	X	✓
Nigeria	✓	X	X	NA
Panama	X	X	✓	✓
Russia	X	X	X	X
Singapore	✓	X	✓	✓
Switzerland	✓	✓	✓	✓
Thailand	X	X	X	X
Turkey	X	X	X	X
Britain	✓	✓	✓	✓
United States	✓	✓	✓	✓
Venezuela	✓	X	✓	✓

A - banks required (or permitted) to report suspicious transactions

B - Government permits sharing of seized assets with other governments that assisted the underlying investigation

C - Non-banks must meet same anti-laundering provisions as banks

D - Financial institutions and employees who provide otherwise confidential data to investigators pursuing authorised investigations are protected from prosecution

Source: US Department of State (International Narcotics Control Strategy Report)

5. Financial Sector reforms in Singapore

Banking	*Insurance*	*Fund Management*	*Equity and Futures Markets*	*Bond Market*
Raised Bank Disclosure Standards Discontinue practice of Maintaining hidden reserves. Provide details on loan loss provisions. Disclose off-balance sheet Items in notes to accounts. Disclose significant exposures. Clarified and Liberalised Guidelines on S$ Loans for Regionalisation	Liberalised Investment Limits on Singapore General Insurance and Non-Investment-Linked Life Insurance Funds Put in Place Easier Operating Environment for Captive Insurers Reduced paid-up capital requirement from $1 mn to $400,000. Captive insurers allowed to	Committed to Place Out $25bn of GIC Funds and $10 bn of MAS Funds Over Next 3 Years for External Fund Managers to Manage GIC placed out $6.5 bn as at September 1998. Revamped CPF Investment Scheme Set new selection criteria for CPF-approved fund managers. Set new investment guidelines and introduced disclosure Requirements for CPF-approved unit trusts.	Eased Conditions for Foreign Companies to List in S$ on the SES (See MAS 757) Removed Limit on Investments in Foreign Currency-Denominated Shares by CPF-Approved Unit Trusts Launched New Equity Derivative Contracts SIMEX launched MSCI Singapore Stock Index Futures (in September 98) and Dow Jones Thailand Stock Index Futures (in November 98).	Increased Government Debt Issues and Announced a Regular Calendar of Issues Issued $1.5 bn of 10-year Singapore Government Securities (SGS). Increased Bond Issues by Statutory Boards like JTC, PUB, and HDB JTC launched $4 bn medium-term note programme. HDB announced plans to issue $2 bn worth of bonds.

Projects Lowered Minimum Cash Balance (MCB) from 6% to 3% Raised Limits on Offshore Banks' S$ Loans to Residents from$200 mn to $300mn Launched Real Time Gross Settlement System for Inter bank Payments Facilitated Regulatory Co-operation Made it easier for foreign regulators to inspect Singapore branches of their banks Allowed foreign banks to disclose information on Credit facilities to their parent supervisory	Write prescribed non in-house risks. Enhanced Tax Incentives Extended 10-year tax exemption for Singapore-registered insurers in respect of income from offshore marine hull and liability business.	Liberalised Guidelines for Non-CPF Unit Trusts Introduced new investment, borrowing and advertising guidelines. Removed minimum investment requirements for unit trust regular savings plans. Reduced Entry Requirements for Foreign Companies Setting Up as Investment Advisers in Singapore Reduced minimum Shareholders' funds from $500 mn to $100 mn. Reduced minimum global Funds managed by parent Company from $5 bn to $1 bn.	SIMEX relaunched MSCI Hong Kong Stock Index Futures in November 98. Widened Scope of Activities for Stockbrokers Reviewed SIMEX membership structure to allow SES members to apply for SIMEX membership so as to market and trade SIMEX's equity index contracts. Facilitated applications by Stockbroking firms for investment adviser licences. Introduced New Best Practices Guide on Audit Committees and Dealing in Securities	Allowed Foreign Entities to Issue S$-Denominated Bonds in Singapore (See MAS 757) International Finance Corporation launched the first AAA S$ bond issued by a Foreign borrower in October 98. Allowed Banks to Transact S$ Repurchase Agreements of up to $20 mn with Non-Bank Non-Residents Allowed Banks to Transact S$ Currency and Interest Rate Swaps with Special Purpose Vehicles for

authorities.		Enhanced Tax Incentives Abolished withholding tax on unit trust distributions. Extended tax exemption to unit holders' distributions made out of capital gains. Exempted from tax fund Managers who manage more than $5 bn in Singapore.	Legalised Share Buy-Backs Commenced Inspection of Securities Market Intermediaries Enhanced Tax Incentives Extended certain tax incentives for venture capital funds for a further 5 years beyond the current maximum of 10 years. Renewed tax holiday for SIMEX for another 5 years. Suspended stamp duty on Securities transactions for 1 year w.e.f. 30 Jun 98.	Securitising Mortgages Allowed CPF-Approved Unit Trusts to Invest in High Grade Bonds Introduced Tax Incentives to Encourage Origination and Trading of Debt Securities in Singapore

Implement Risk-focused Approach to Bank Examinations Conduct more focused and Regular inspections to distinguish stronger banks from weaker ones.	Review Investment Guidelines for Investment-Linked Insurance Policies Enhance Operating Environment for Captive Insurers Introduce New Reinsurance Products Study the actuarial and Accounting issues relating to the introduction of specialised pioneer products such as alternative risk transfer products.	Consolidate Unit Trust Regulation in MAS Review Trustees Act Relax investment restrictions on statutory boards, private pension funds and authorised unit trusts. Delink investment limits under CPFIS from Trustees Act. Put in place regulatory framework for private pension funds. Introduce Regulatory Framework for independent Financial Advisers Introduce Code of Ethics for Fund Managers Create Conducive	Progressively Deregulate Commission Rates Progressively Open Up to Foreign Participation in the Stock-broking Industry Liberalise Employee Share Option (ESOP) Schemes Widen Product Range in Equity Market Expand the SES options market by introducing options on more stocks. Introduce new products (e.g. stock index options, country basket of shares, listed property trusts/real estate investment trusts). Develop an electronic bulletin board/organised	Promote Asset-Backed Securities Market Resolve legal and regulatory issues relating to asset-backed securities. HDB is considering the issuance of mortgage-backed securities. Introduce Regulatory Guidelines for underwriters and dealers and Trading Rules for Debt Securities Develop Efficient Clearing System for Corporate Bonds

		Environment for Indigenous Boutique Fund Managers Introduce Training Programmes to Develop Local Fund Management Expertise	OTC market on SES for trading foreign securities. Demutualise and merge SES and SIMEX Shift from Merit-Based Regulation Towards Predominantly Disclosure-Based Regulation Consolidate Securities Regulation in MAS to Reduce Duplication and Improve Efficiency	

MISSION STATEMENT

Bombay First is an initiative to make the city a better place to live, work and invest in. It aims to serve the city with the best that private business can offer. It will achieve this by addressing the problems of today and the opportunities of tomorrow, through partnerships with government, business and civil society

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