CHAPTER

22

ECONOMIC CONCEPTS AND TERMINOLOGIES

(Reference to Selected Terms Related to Economic and Indian Economy)

*Concepts are the constituents of thoughts–consequently, they are crucial to such psychological processes as categorization, inference, memory, learning, and decision-making.**

* *See Eric Margolis and Stephen Laurence, 'Concepts', in the Edward N. Zalta* ***The Stanford Encyclopedia of Philosophy,*** Metaphysics Research Lab, Centre for the Study of Language and Information (CSLI), *Stanford, USA, 2012.*

ACCRUAL BASIS

An accounting method which considers revenues and expenses as they accrue, even though cash would not have been received or paid during the period of accrual.

ACTIVITY RATE

The labour force of a country is known as the activity rate or *participation rate*. It is in per cent and always a proportion of the total population of the country—the economically active population. This rate varies from one country to another depending upon several factors such as school leaving age, retirement age, popularity of higher education, social customs, opportunities, etc.

ADRS

ADR stands for American Depository Receipt, which enables investors based in the USA to invest in stocks of non—US companies trading on a non the US stock exchange. ADRs are denominated in dollars. Simply put, US brokers purchase shares of a foreign company, say Infosys (on behalf of their clients). ADRs are subsequently listed on US stock exchanges.

ADRs can be sponsored or unsponsored. Sponsored ADRs are those in which the company actively participates in the process. Sponsored ADRs can be Level I, Level II or Level III. There are also what are called Rule 144A. The ADRs were first offered in the US in the 1920s. A number of Indian companies have issued ADRs. Infosys Technologies was the *first* Indian company to use the ADR route.

The terms *ADR* and *ADS* are often used interchangeably. The individual shares representeted by an ADR are called American Depositary Shares (ADS).

To the company issuing ADRs, it provides access to the American market. A company can, therefore, raise additional resources. To an American investor, it provides the opportunity to invest in stock of companies not listed in the US. Huge operational, custodial, and currency conversion issues can come into play if the ADR route is not used.

ADS CONVERSION OFFER

Conversion of local shares into American Depository Shares (ADS) of a company is called an ADS conversion offer. It is managed by investment bankers, mainly large investment banks familiar with Indian and global markets The offer allows local investors to convert their shares into ADS and then sell it in US markets. The proceeds of the sale in the US markets is distributed to Indian investors in rupees after deduction of expenses incurred in the process. The company does not issue any new shares. Existing shares are converted into ADS. The scheme obviously can only be offered by companies listed on the Indian and US markets which is the case for many large Indian corporates.

American Depository Shares are usually traded at a premium to the underlying (Indian) share price.

If the share conversion offer takes place through the stock market in India, investors pay no long-term capital gains tax. A 10 per cent short-term capital gains tax is applicable. Investors, however, have to pay the securities transaction tax in the process. However, if the offer is not through the stock market system, then investors have to pay 30 per cent short-term capital gains tax with surcharge or 10 per cent long-term capital gains tax as applicable. Investors do not have to pay any securities transaction tax.

Companies do not issue new shares. Thus, the offer does not lead to any dilution of equity and earnings per share. They are making this offer to satisfy the demand for ADS traded in US markets. This allows companies to have new investors and creates visibility on the US stock exchanges. They also satisfy the local investor by offering an opportunity to sell their shares at a higher price than available locally on the Indian bourses.

ADVERSE SELECTION

One among the two kinds of the market failure often associated with insurance business which means doing business with the people one would have better avoided.

Adverse selection can be a problem when there is an asymmetry in information between the seller and the buyer of an insurance policy—as insurance will not be profitable when buyers have better information about their risk of claiming than does the seller of the insurance policy. In the ideal case, insurance premiums are set in accordance to the risk of a randomly selected person in the insured bracket (such as 40-year-old male smokers) of the population.

The other kind of market failure is *moral hazards* associated with the insurance sector.

AGRICULTURAL EXTENSION

Agricultural extension is a proper approach to motivate people to help themselves by applying agricultural research and development in their daily lives in farming, home making, and community living. It plays a vital role in community development. It is a two-way channel that brings scientific information to rural people and takes their problems to scientific institutes (for further research and development) for their solution.

In India, like many other developing countries, the role of agricultural extension is more than educational and it needs to deal with the human resource development of the agrarian population too, making it a comparatively tougher task than in the developed countries. The spread of information technology will serve a great purpose in this area.

AGRICULTURAL LABOURER

A person who works on another person's land for *wages* in money or kind or share is regarded as an agricultural labourer. He or she has no risk in the cultivation, but merely works on another person's land for wages. An agricultural labourer has no right of lease or contract on land on which he/she works.

AGRICULTURAL MARKETS

Agricultural Markets are regulated and managed under the Agricultural Produce Market Act (APMC Act) enacted by the respective state governments. The Central government provides guidance and assistance in regulation and development of agricultural-produce markets. 7,521 markets have been brought under regulation upto March this year. To handle increasing quantity, more and more markets have been brought under regulation over the years. There were only 286 regulated markets in 1950 on an average. a regulated market serves 459 sq. km. but the National Commission on Agriculture recommended that a regulated market should serve farmers within a 5 km radius and a command area of 80 sq. km.

ALPINE CONVERTIBLE BOND

An ACB (Alpine Convertible Bond) is a Foreign Currency Convertible Bond (FCCB) issued by an Indian company exclusively to the Swiss investors.

AMMORTISATION

Payment of a loan in installments by the borrower. It is usually done in an agreed period and every installment includes a part of the total loan plus the interest.

ANDEAN PACT

A regional pact to establish a common market link, started originally in 1969. At present it has peru, Equador, Columbia, Bolivia, and Venezuela. The pact had almost collapsed by the mid-1980s due to regional, economic, and political instabilities and was re-launched in 1990 (the original member Chile was dropped and the new member venezuela was added to it).

ANIMAL SPIRIT

'Confidence', considered as one of the essential ingredients of economic prosperity was called by J. M. Keynes as animal spirit. For keynes, this is a 'naive optimism' by which an entrepreneur puts aside the fact of loss as a healthy man puts aside the expectation of death.

But from where does this animal spirit come has been a mystery—can it be created artificially from outside or whether it is an innate thing some are born with, etc.

ANTITRUST

A category of the government policy which deals with monopoly. Such laws intend to stop abuses of 'market power' by big companies and at times to prevent corporate mergers and acquisitions that would strengthen monopoly. The US has such laws and recently it was in news when Microsoft was its target.

APPRECIATION

It shows increase in value and is used in economics in the following two senses:

(i) It is an increase in the price of an asset over time, such as price rises in land, factory building, houses, offices, etc. It is also known as *capital appreciation.*

(ii) It is an increase in the value of currency against any foreign currency or currencies. It is market-based if the economy follows the floating-currency exchange-rate system.

ARBITRAGE

Earning profits out of the price differences of the same product in different markets at the same time. For example, buying and selling any product, financial securities (as bonds) or foreign currencies in different markets/economies. As globalisation is promoting liberalised cross-border movement of goods and services around the world, arbitrage is prevalent today. To avoid arbitrage the WTO member countries (i.e.) the official countries in the process of globalisation) are under compulsion to chalk out homogenous economic policies–and a level-playing field at the international level is emerging.

ARCS

Assets Reconstruction Companies (ARCs) acquire non-performing assets (NPAs) from banks or financial institutions along with the underlying securities mortgaged and/or hypothecated by the borrowers to the lenders. The ARCs then try and manage or resolve these NPAs acquired from banks. It can even infuse more funds in order to reconstruct the asset. If reconstruction is not possible and the borrower is unwilling to repay the loan, the ARCs *even sell* the secured assets.

While the basic principle of ARCs is the same everywhere—to acquire bad loans to resolve them—the essential difference is in the ownership of ARCs, public or private. After the Asian Crisis, countries like Indonesia, Korea, Malaysia, and Thailand have adopted government-owned and funded ARCs. The Philippines, on the other hand, has opted for private ARCs. India, too, has adopted the private sector model of asset resolution. Here, ARCs are set up as non-governmental vehicles mostly with support from the banking sector and other investors. Also, India has opted for multiple ARCs, which helps in better pricing of bad loans, as opposed to the single ARC model followed in many countries. The RBI has already allowed licenses to three ARCs and some banks are also planning to float ARCs.

ARCs acquire NPAs by way of 'true sale', i.e., once an NPA has been sold, the seller has no further interest in that asset.

ARCs are a product of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (**SARFAESI Act**). And they derive their asset resolution powers from this Act. The act provides full right to the lenders acting in majority (75 per cent of the total debt by value) to enforce the security in tersest (terms of the loan) without judicial intervention. Through buying out major lenders in a loan gone bad (to the extent of 75 per cent of value), through the mechanism mentioned earlier, an ARC is able to have recourse to SARFAESI Act and, thereby, acquire legal muscle to force settlement.

It is true that if a bank itself has 75 per cent of the total value of debt in an NPA or is able to buy out other and accumulate the same, then it also gets recourse to SARFAESI. In that sense, banks are at par with ARCs. That is why we now find that some banks are getting interest and acquiring bad assets, just like an ARC does. However, a bank's business is not to deal bad assets or try and reconstruct them. An ARC, on the other hand, is in the business of reconstructing bad assets, and has acquired skill and experience in asset resolution. It is able to do the same job better. Moreover, selling an NPA helps a bank to clean its balance sheet, too.

ASSET

Anything which has a 'money value' owned by an individual or a firm is an asset. It is of *three* types:

(i) *Tangible Asset:* All physical assets such as land, machinery, building, consumer durables (refrigerator, car, TV, Radio, etc.), etc. (*the assets which are in the material form*).

(ii) *Intangible Assets:* All non-physical/ immaterial assets such as brand names, good-will, credit-worthiness, knowledge, know-how, etc.

(iii) *Financial Assets:* All financially valid valuables other than tangibles and intangibles such as currencies, bank deposits, bonds, securities, shares, etc.

ASSIGNED REVENUE

The term is used to refer to various tax/duty/ cess/surcharge/levy etc., proceeds of which are (traditionally) collected by state government (on behalf of) local bodies (the PRIs), and subsequently adjusted with / assigned to the PRIs. Collection of such revenue is governed by relevant Acts of the local bodies.

Some examples of assigned revenue in India, include, entertainment tax, surcharge on stamp duty, local cess/surcharge on land revenue, lease amount of mines and minerals, sale proceeds of social forestry plantations, etc. State Finance Commissions recommend *devolution* of assigned revenue to local bodies on objective criteria, which may be specified by them in specific context.

AUTARKY

The idea of self-sufficiency and 'no' international trade by a country. None of the countries of the world has been able to produce all the goods and services required by its population at competitive prices, however, some tried to live it up at the cost of inefficiency and comparative poverty.

BACKWARDATION

A term of future trading which means a commodity is valued higher today (i.e., spots market) than in the futures (i.e., future market). When the situation is opposite, it is known as *contango*.

BACK-TO-BACK LOAN

A term of international banking, is an arrangement under which two firms (i.e., companies) in different economies (i.e., countries) borrow each other's currency and agree to repay (such loans) at a specified future date. Each company gets full amount of the loan on the repayment date in their domestic currency without any risk of losses due to exchange rate fluctuations. It has developed as a popular tool of minimising the exchange-rate exposure risk among the multi-national companies. This is also known as the *parallel loan*.

BAD DEBT

An accounting term to show the loans which are unlikely to be paid back by the borrower as the borrower has become insolvent/bankrupt. Banks might write off such bad debts against the profits of the trading as a business cost.

BADLA

An Indian term for 'contango' associated with the trading system in the stock market which is a postponement of either payments by the share buyer, or the person who needs to deliver the shares against the payment.

BALANCED BUDGET

The annual financial statement (i.e., the budget) of a government which has the total expenditures equal to the taxes and other receipts.

Most governments, in practice run unbalanced budgets, i.e., deficit budgets or surplus budgets– either the expenditures being higher or lower than the taxes and the other receipts, respectively. It is done to regulate the economic activities.

BALANCE OF PAYMENTS

A balance sheet of an economy showing its total external transactions with the world– calculated on the principles of accounting–is an annual concept.

BALLOON PAYMENT

When the final payment of a debt is more than the previous payments, it is balloon payment.

BASING POINT PRICE SYSTEM

A method of pricing in which a differential (i.e., varying) price is fixed for the same product for the customers of the different locations—nearer the customer, cheaper the product. This is done usually to neutralise the transportation cost of the bulky products such as cement, iron and steel, petroleum, etc.

BELLWETHER STOCK

A share which often reflects the state of the whole stock market. The technical analysts, associated with the stock market, usually keep a track-record of such shares and go on to forecast the future stock movements.

BFS

For the purpose of supervision and surveillance of the Indian financial system, a Board for Financial Supervision (BFS) was set up by the RBI in November 1994. The board supervises commercial banks, non-banking financial companies

(NBFCs), financial institutions, primary dealers, and the clearing corporation of India (CCI).

BLACK-SCHOLES

A formula devised for the pricing of financial derivatives or options—made explosive growth possible in them by the early 1970s in the US.

Myron Scholes and Robert Merton were awarded Nobel Prize for Economics for their part in devising this formula—the co-inventor fischer Black had died (1995) by then.

BOND

An instrument of raising long-term debt on which the bond-issuer pays a periodic interest (known as *'coupon'*). In theory, bonds could be issued by governments as well as private companies.

Bonds generally have a maturity period, however, some bonds might not have any definite maturity period (which are known as *'Perpetual Bonds'*).

Bonds are supported/secured by collateral in the form of immovable property (i.e., fixed assets) while *debentures,* also used to raise long-term debt, are not supported by any collateral.

BOOK BUILDING

This is a public offer of equity shares of a company. In this process, bids are collected from the investors, in a certain price range fixed by the company. The issue price is fixed after the bid closing date depending on the number of bids received at various price levels. A company that is planning an initial public offer (IPO) appoints a merchant banker as a 'book runner'. The company issues a prospectus which does not mention the price, but gives other details about the company with regard to issue size, the business the company is in, promotes and future plans among other disclosures. A particular period is fixed as the bid period. The book runner builds an order book, that is, collates the bids from various investors, which shows the demand for the shares. Prospective investors can revise their bid at any time during the bid period. On closure of the book, the quantum of shares ordered and the perspective prices offered are known. The price discovery is a function of demand at various prices, and involves negotiations between those involved in the issue. The book runner and the company conclude the pricing and decide the allocation to each member.

BRACKET CREEP

Increasing incomes due to inflation (via increased dearness allowances, individual income goes for an increase) pushes individuals into higher tax *brackets* and leaves them worse off (as their real income has not increased and their disposable income i.e. income after tax payments, falls) – this phenomenon is known as the bracket creep.

BROAD BASED FUND

This is a fund established or incorporated *outside* India, which has at least 20 investors with no single individual investor holding more than 49 per cent of the shares or units of the fund. If the broad based fund has institutional investor (s), then it is not necessary for the fund to have 20 investors. Further, if the broad based fund has an institutional investor who holds more than 49 per cent of the shares or units in the fund, then the institutional investor must itself be a *broad based fund.*

In India, the entities, proposing to invest *on behalf of broad based funds*, are eligible to be registered as FIIs are: (i) Asset Management Companies, (ii) Investment Manager/Advisor, (iii) Institutional Portfolio Managers, (iv) Trustee of a Trust, and (v) Bank

BROWNFIELD LOCATION

A derelict industrial area that has been demolished to accommodate new industries. This is opposite to the *greenfield location* where a new industry is set up in a new area.

BUBBLE

The price rise of an asset unexplained by the fundamentals and still people interested in holding the assets. After the bursting of the bubble, assets cool down to their real prices.

BUDGET LINE

A line on the dual axis graph showing the alternate combinations of goods that can be purchased by a consumer with a given income at given prices.

BULLET REPAYMENT

'Bullet repayment' means a lump-sum payment for the *entire loan amount* paid at the time of maturity. Such arrangements may be put in place by the banking regulator (RBI in case of India) to fasten the process of recovery of the non-performings assets (NPAs) process of the banks. The distressed assests, in this way come back to bank, may be with a lower profit element to them.

Such an announcement was made by the RBI in 2014–15 allowing *bullet repayment* of loans extended against pledge of gold ornaments and jewellery for other than agricultural purposes.

BULLION

Precious metals such as gold, silver, and platinum that are traded in the form of *bars* and *coins* for investment purposes and are used for jewellery as base metals.

BUSINESS CYCLE

See the chapter with the same title.

BUSY & SLACK SEASONS

The monetary authorities face the challenge of keeping the growth rate as high as possible, at the same time putting burden of adjustment on luxury and unproductive consumption. Monetary policy is an instrument in this respect. However, the right policies may not be palatable to the political and fiscal authorities, which is a serious problem for the economy.

From May beginning to end-September is the *slack season* and from October beginning to end-April is the *busy season* of the ***Indian economy***. During the slack season, crops are generally sown. Agriculture and related businesses are slack and loans taken during the previous busy season tend to be returned. Consequently, the growth rate of money is low or negative. Governments usually borrow heavily during the slack season, since the demand for credit from the commercial sector is not very strong. Since there are no fresh crop arrivals in the market and the demand for crops is steady, the prices are expected to be generally upward in the slack season.

From October, the busy season commences and both agricultural and related industrial productions are high. Since crops arrive in the market during the busy season, prices generally are on the downward drift. It is the seasonal variation in the arrival of crops in the market, in the context of steady demand, that causes prices to fluctuate during the year.

The above pattern has been severely modified in recent years. The government borrows both during the slack and the busy seasons. Industry too is active in both the seasons. Because of greater storage and stocking facilities, the variations in the flows o f agricultural products have been reduced. Money supply expands continuously and prices are generally up throughout.

BUYER'S MARKET

A short period of market situation in which there is excess supply of goods/services forcing price fall to the advantage of the buyers.

BUYOUTS

Private equity (PE) investors participate in two types of buyouts of firms (a PE-backed buyout simply means that the PE investor takes a controlling stake i.e. between 50–100 per cent in a company):

(i) *Management Buyout (MBO):* In such buyouts, the PE investor usually helps the existing management of the company to buy out the promoters of the company. In return, the PE investor takes a majority stake.

(ii) *Leveraged Buyout (LBO):* In such buyouts, a large portion of fund in acquiring the company is financed by debt–the normal ratio being 70 per cent debt and 30 per cent equity.

CAMELS

An acronym derived from the terms capital adequacy (C), asset quality (A), management (M), earnings (E), liquidity (L) and systems for control (S). The acronym is used as a technique for evaluating and rating the operations and performance of banks all over the world.

CAPITAL

Capital is one of the three main factors of production (*labour* and *natural resources* are the other two), classified into *physical capital* (i.e., factories, machines, office, etc.) and *human capital* (i.e., training, skill, etc.).

In a joint stock company, the capital has various specific terms showing different forms of the *share capital:*

(i) *Authorised Capital:* This is the amount of share capital fixed in the Memorandum of Association (MoA) and the article of association of a company as required by the Companies Act. This is also known as the *Nominal* or *Registered Capital.*

This is the limit (i.e., nominal value) upto which a company can issue shares. Companies often extend their authorised capital (via an amendment in the MoA) in advance of actual issue of new shares. This allows the timing of capital issue to be fixed in light of the company's need for new capital and the state of the capital market and allows share options to be excercised accordingly.

(ii) *Paid-up Capital:* The part of the authorised capital of a company that has actually been paid up by the shareholders. A difference may arise because all shares authorised may not have been issued or the issued shares have been only partly paid-up by then.

(iii) *Subscribed Capital:* The capital that has actually been paid by the shareholders (as they might have committed more than this to contribute). It means, the subscribed capital is the actually realised paid-up capital (paid-up capital is subscribed capital plus credit/due on the shareholders).

(iv) *Issued Capital:* The amount of the capital which has been sought by a company to be raised by the issue of shares (it should be kept in mind that this cannot exceed the authorised capital).

(v) *Called-up Capital:* The amount of share capital the shareholders have been *called* to pay to date under the phased payment terms. It is usually equal to the 'paid-up capital' of the company except where some shareholders have failed to pay their due installments (known as *calls in arrears*).

CAPITAL ADEQUACY RATIO

A regulation on commercial banks, co-operative banks and the non-banking financial companies to maintain a certain amount of capital in relation to their assets (i.e., loans and investments) as a cushion (shock-absorber) against probable losses in their investments and loans.

A concept devised by the Bank for International Settlements (BIS), Basel, the provision was implemented in India in 1992 by the RBI (for more detailed discussion see the chapter on 'Banking').

CAPITAL CONSUMPTION

The capital that is consumed by an economy or a firm in the production process. Also known as *depreciation*.

CAPITAL-OUTPUT RATIO

A measure of how much additional capital is needed to produce each extra unit of the output. Put the other way round, it is the amount of extra output produced by each unit of added capital. The ratio indicates how efficient new investment is in contributing to the growth of an economy.

A capital-output ratio of 3:1 is better to the 4:1 as the former needs only three units extra capital to produce one extra output in comparison to the latter which needs four units for each extra unit output.

CARBON CREDIT

Amidst growing concern and increasing awareness on the need for pollution control, the concept of carbon credit came into vogue as part of an international agreement, known popularly as the Kyoto Protocol. Carbon credits are certificates issued to countries that reduce their emission of GHG (greenhouse gases) which leads to global warming. It is estimated that 60–70 per cent of the GHG emission is through fuel combustion in industries like cement, steel, textiles, and fertilisers. Some GHGs like hydro fluorocarbons, methane, and nitrous oxide are released as byproducts of certain industrial process which adversely affect the ozone layer, leading to global warming.

Kyoto Protocol is a voluntary treaty signed by 141 countries including the European Union, Japan, and Canada for reducing GHG emission by 5.2 per cent below 1990 levels by 2012. However, the US, which accounts for one-third of the total GHG emission is yet to sign this treaty. The preliminary phase of Kyoto Protocol started in 2007 while the second phase starts from 2008. The penalty for non-compliance in the first phase is 40 euro per tonne of Co_2 equivalent and in the second phase the penalty will be hiked to 100 euros per tonne of Co_2.

The Kyoto Protocol provides for *three* mechanisms that enable developed countries with quantified emission limitation and reduction commitments to acquire greenhouse gas reduction credits. These mechanisms are Joint Implementation (JI), Clean Development Mechanism (CDM) and International Emission Trading (IET). Under *JI,* a developed country with a relatively higher costs of domestic greenhouse reduction sets up a project in another developed country which has a relatively low cost. Under *CDM,* a developed country can take up a greenhouse gas reduction project activity in a developing country where the cost of GHG reduction project activities is usually much lower. The developed country would be given credits for meetings its emission reduction target, while the developing country would receive the capital and clean technology to implement the project. Under *IET* mechanisms, countries can trade in the international carbon credit market. Countries with surplus credits can sell the same to those with quantified emission limitation and reduction commitments under the Kyoto Protocol.

The concept of carbon credit trading seeks to encourage countries to reduce their GHG emissions, as it rewards those countries which meet their targets and provides financial incentives to the others to do so as quickly as possible. Surplus credits (collected by overshooting the emission reducing target) can be sold in the global market. One credit is equivalent to one tonne of Co_2 emission reduced. Carbon Credit (CC) is available for companies engaged in developing renewable energy projects that offset the use of fossil fields. Developed countries have to spend nearly $25 billion which will be ultimately spent by developing countries. In countries like *India,* GHG emission is much below the target fixed by Kyoto Protocol and so, they are excluded from reduction of GHG emission. On the contrary, they are entitled to sell surplus credits to developed countries. It is here that trading takes place. Foreign companies, who cannot fulfill the protocol norms, can buy the surplus credit from companies in other countries through trading. Thus, the stage is set for Credit Emission Reduction (CER) trade to flourish. India is considered as the *largest* beneficiary claming about 31 per cent of the total world carbon trade through the Clean Development Mechanism (CDM).

The trading takes place on two stock exchanges, the Chicago Climate Exchange and the European Climate Exchange. CC trading can also take place in the open market as well. European countries and Japan are the major buyers of carbon credit. Under the Kyoto Protocol, global warming potential (GWP) is an *index* that allows for the comparison of greenhouse gases with each other in the context of the relative potential to contribute to global warming. For trading purposes, one credit is considered equivalent to one tonne of Co_2 emission reduced.

Getting carbon credits certified for Kyoto is a rather lengthy and complex process. There are four stages of CDM approval. First stage is at the domestic level where the project gets approved by National CDM Authority (NCM). After NCM's approval the project is sent to the United Nations Framework Convention on Climate Changes. After this the executive board of UNFCCC reviews the project. The project gets evaluated on every front and is then registered under UN FCCC only if it meets all the norms. Thereafter, certification is done for the reduction in emission and credits are issued.

CARRY TRADE

Borrowing in one currency and investing in another is termed as carry trade. In recent times (upto November 2007) trillions of dollars have been borrowed in low-cost 'yen' for deployment across money markets, stock markets, and even real estate markets across the globe and a part of the money flowed into India, too.

In recent months, Japan has been the best market for 'carry trades' because of a weak Yen and a cost of borrowing that is almost 'zero'; in seven years since 1999, and after two hikes by the Bank of Japan, the interest rate is 0.5 per cent. The money thus borrowed is usually invested in the respective currencies in markets where the interest rate is higher, or in equities. Preferred destinations include the USA, N. Zealand, and Australia for debt investments, and emerging markets such as India for equity investment.

CASH COW

A profitable business or firm (may belong to either public or private sector) which gives regular cash flow to the owner (this happens either due to regular demand of the popular goods produced by the firm or the compulsions of the consumer to buy the products). As for example, the antiseptic lotion 'Dettol' is a cash cow for Reckitt and Colman in the private sector and LPG is a cash cow for the manufacturing and marketing government companies (provided there is no subsidy on LPG).

CAVEAT EMPTOR

A Latin phrase which means *'let the buyer beware'*. Simply put, it means that the supplier has no legal obligation to inform buyers about any defects in his goods or services; the onus is on the buyer to himself determine the level of satisfaction out of the products.

CETERIS PARIBUS

A Latin phrase which means *'other things being equal'*. The phrase is used by economists to cover their forecastings.

CHINESE WALL

The segregation of the different activities of a financial institution (such as, jobbing, stockbroking, fund management, etc.) in order to protect clients' interest.

CIRCUIT LIMIT

A limit of regular fall in share indices of Stock Exchanges around the world after which the exchange are closed for further trading. For example, circuit limit decided for the BSE (Bombay Stock Exchange) has been fixed at 10 per cent. The time there is a continuous fall in the BSE Sensex and it reaches 10 per cent, the exchange is closed to further trading.

Such a limit/provision prevents the share market from crashing down.

CLASSICAL ECONOMICS

A school of thought in economics based on the ideas of Smith, Ricardo, Mill, etc. The school dominated the economic thinking of the world until about 1870, when the *'marginalist revolution'* took place.

CLEAN COAL

Underground coal gasification and liquefaction which converts coal into liquid and gaseous fuel alternatives is a recognised 'clean coal' technology—handy in extraction of energy from coal seams which connot be mined through conventional methods.

CLOSED SHOP

The requirement that all employees of a given firm be members of a specified trade union. It is a method of restricting labour supply and maintaining high wages applied by a powerful trade union.

COLLECTIVE PRODUCTS

A product which can only be supplied to a group. Many goods and services provided by the governments fall in this category, such as, national defence, police administration, etc.

COMMODITIES TRANSACTION TAX

[See Chapter 17, *Tax Structure in India*]

COMMODITY MONEY

Products being used as the means of payment as in the traditional barter system. Such practices take place generally when the confidence in money has fell down (as for example in the situations of high inflation and high depreciation).

COMMUNITISATION

A method of privatising public service delivery without going for the tendering process. It is done by transfering powers including financial powers to the user community who will take up the job of revenue collection along with an effective and more practical governance of the service delivery. This model is bereft of profit motive and so, more transparent.

Service delivery in communitised elementary schools and health service institutions has improved considerably and power tariff collection has risen by 100 per cent since the reform began in 2002 in Nagaland—Secretary, Union Ministry of Steel, Raghaw Sharan Pandey who did it in Nagaland as its chief secretary.

COMPARATIVE ADVANTAGE

It is about identifying activities that an individual, a firm or a country can do most efficiently, being together.

The idea, usually credited to David Ricardo, underpins the case of free trade. It suggests that countries can gain from trading with each other even if one among them is more efficient (i.e., it has an *absolute advantage*) in every kind of economic activity.

CONSOLS

This is the abbreviated form of *consolidated stock*. The government bonds which have no maturity and thus have an indefinite life–are tradable on the floors of the stock exchanges.

CONSORTIUM

An *ad hoc* grouping of firms, governments, etc. brought together to undertake a particular project by pooling their resources and skills for major construction projects, loans, etc.

CONSUMER DURABLES

Consumer goods that are consumed over relatively long periods of time rather than immediately (opposite to the *consumer non-durables*) such as cars, houses, refrigerators, etc.

CONSUMER NON-DURABLES

Consumer goods which yield up all their satisfaction/utility at the time of consumption (Opposite to the *consumer durables*), examples are cheese, pickles, jam, etc.

CONSPICUOUS CONSUMPTION

Consumption for the purpose of showing off ostentatiousness but not for the utility aspect – for example, the use of diamond-studded sandals, watches, pens, etc.

CONTAGION

A situation or an effect of economic problems in one economy spreading to another also known as the *domino effect*.

CONTRARIAN

A person following an investment strategy (specially in share market) just opposite to the general investors in a given period. For example, when a share is generally being sold by the investors, a contrarion keeps on buying them—

the logic is that due to selling pressure the price will fall below the intrinsic value of the share and there is a prospect of future profit out of the share.

CORE INVESTMENT COMPANIES (CICS)

A NBFC carrying on the business of acquisition of shares and securities which satisfied the conditions: it holds not less than 90 per cent of its total assets in this form; its investments in the equity shares in group companies constitutes not less than 60 per cent of its total assets; it does not trade in its investments in shares, debt or loans in group companies except through block sale for the purpose of dilution or disinvestment; and it does not carry on any other financial activity except investment in bank deposits, money market instruments, government securities, loans to and investments in group companies.

CORPORATE SUSTAINIBILITY INDEX

The Bombay stock Exchange (BSE) has proposed to come out with a corporate sustainability index (CSI)—a possible new stock exchange which will be created for developing *trust marks* to denote a corporate's sustainability achievements. This will be the first such index in Asia.

CORRECTION

A term usually used in stock market which shows a reversals of share prices in reaction to an excessive rise or fall of the past.

CREATIVE DESTRUCTION

The process by which an innovative entrepreneur takes risks and introduces new technologies to stimulate economic activity, replacing old technologies is known as 'creative destruction'. As per *Schumpeter, Joseph A.* (1883–1950), creative destruction is the key to economic growth. But due to irregularity in such innovations, business cycle is followed by both collapse and crisis (J. A. Schumpeter, *capitalism, Socialism and Democracy,* 1942).

CRONY CAPITALISM

An approach of doing business when the firms look after themselves by looking after their own people (i.e., families and friends). Used in negative sense.

CROSS SUBSIDY

The process of giving subsidy to one sub-area and fulfilling it through the profits from the other sub-area. As for example, in India kerosene oil is cross-subsidised against petrol and aviation fuel.

CROWDING-OUT EFFECT

A concept of public finance which means an increase in the government expenditure which has an effect of reducing the private sector expenditure.

CSR

The concept of corporate social responsibility (CSR) is fast gaining popularity among the corporate sector of the world. As per the experts, the CSR is qualitatively different from the traditional concept of passive philanthropy by the corporate houses. Basically, the CSR acknowledges the *debt* that the corporates owe to the community within which they operate. It defines the corporates' partnership with social action groups (i.e., the NGOs) in providing financial and other resources to support development plans, especially among disadvantaged communities. There is stress on long-term sustainability of business and environment and the distribution of well-being.

DEBENTURE

An instrument of raising long-term loan by companies, having a maturity period bearing an interest (*coupon rate*). Theoretically they may be secured or unsecured by assets such as land and buildings of the issuing company (known as *collateral*).

Debenture holders are provided with a prior claim on the earnings (by interest) and assets of the company in the situation of liquidation of the company over the *preference* and *equity shareholders* of the company.

DEBT RECOVERY TRIBUNAL (DRT)

Banks and financial institutions have often faced a tough time in recovering loans, on which the borrowers have defaulted. To expedite the recovery process, the Committee on the Financial System, headed by *Mr. Narasimham* considered the setting up of special tribunals, with special adjudicator powers. This was felt to be necessary to carry through financial sector reforms. Since there is an immense overload on the Indian legal system at present, recovery of many unpaid debts, due to banks or financial institutions, are held up, indefinitely. This affects the balance sheets of the banks as the amounts involved are very large.

It was thought that an independent forum was needed to deal with debts of these types. Thus, in *1993* the *Recovery of Debts Due to Banks and Financial Institutions Act'* was passed. The Act, however, imposes a limitation and states that only those debts which are in excess of Rs. 10 lakhs (or upto Rs. 1 lakh, where the Central government specified certain types of debts) would come under its purview.

The tribunals are set up by the Central government. The government also specified the areas within which such tribunals will have jurisdiction. A DRT consists of the Presiding Officer to be appointed by notification by the Central government. The government may also specify that the presiding officer of one tribunal may takeover the functions of the presiding officer of another tribunal. A person has to be at least a district judge to become a presiding officer of a Tribunal.

The very first step involved in the recovery process is to make an application to the Tribunal under Section 19 of the Recovery of Debts due to Banks and Financial Institutions Act, 1993. Every bank and financial institution, which stands to recover loans and other debts, shall initiate the procedure by first forwarding an application to the Tribunal within the local limits of whose jurisdiction the defaulter company is located. After the financial institution has filled an application before the Tribunal, and if there are other banks whose loan to the same company has become bad, the latter can join the recovery suit.

DEBT SWAP SCHEME

In 2003, the Government of India announced a scheme to replace the relatively high cost debt of states with lower cost borrowings, taking advantage of falling interest rates. The scheme envisages states pre-paying that portion of their outstanding debt to the Centre on which the interest rate is 13 per cent and more, contracted during the mid-1990s when general interest rates were high.

Of a total stock of Rs. 2,44,000 crore of outstanding Plan loans, Rs. 1,00,000 crore worth of loans bear a coupon rate of 13 per cent and above. Servicing these loans is a major burden for states, many of which are undergoing fiscal stress. These loans from the Centre would be pre-paid using fresh, lower cost debt, which consists of both the small savings lent to the states by the National Small Savings Fund and additional market borrowings. As a result, while the total debt of the states would remain unchanged, the cost of servicing the loans would come down. This is the fiscal benefit to the states.

All collections from small savings, which include post office deposits, Kisan Vikas Patras, National Savings Certificates, and the Public Provident Fund (PPF), flow to the public account.

After adjusting for repayments to the depositors of these small savings instruments, the entire net collections are lent to the states. Of the amount apportioned to each state based on the collection in the respective states, 70 per cent is made available as cash transfer, while the remaining 30 per cent is used for repaying the high cost loans of 13 per cent and above.

Apart from this, states are also now allowed to use additional market borrowings at an average interest rate of less than 6.5 per cent to retire high cost debt.

In simple language, what this means is that while the small savings deposits except for the PPF have a maturity of five to six years, the repayment of loans given to states against small savings is over a period of 25 years. If interest rates were to rise over the medium to long term, this could obviously create a problem for the centre, since the cost of its borrowings would be going up, while the return on its existing loans to the states would remain locked. It is to take care of this risk that the higher spreads is needed.

DECOUPLING THEORY

Decoupling theory holds that Asian economies, especially emerging ones, no longer depend on the United States economy for growth, leaving them *insulated* from a severe slowdown there, even recession—looked true for some time as Asian stocks rose while socks in the US fell - however, as fears of recession mounted in the US, stocks declined heavily. Looking this happen in late 2008 the decoupling theory regarding the Asian as well as the EU economies have now lost ground. But still the emerging economies are able to have higher growth rates and exports in comparision to the US – that is why the theory is still debated by the experts.

DEINDUSTRIALISATION

Sustained decrease in the share of the secondary sector in the total output (GDP) of an economy.

DEMAT ACCOUNT

It is a way of holding securities in electronic or dematerialised form. Demat form of shares can be traded online. As such, the transactions are concluded much faster, which prevents theft, misuse, forging of original shares certificates or other documents, and allows an investor to buy or sell shares in any quantity. Demat account allows for faster refund of money in case application is not accepted. Demat accounts are offered by banks, and the dematerialised stock is held by the depository (National Securities Depository Ltd.–[NSDL] or Central Securities Depository Ltd.–[CSDL]). The investor needs to fill up the requisite forms, submit the documents and pay the applicable charges in order to have the demat account opened.

DEMERGER

The breaking-up of a company into more separate companies. Such companies are usually formed through mergers.

DERIVATIVES

The financial assets that 'derive' their value from other assets, such as shares, debentures, bonds, securities, etc.

DIIS

Domestic Investment Institution (DIIs) are the financial institutions of Indian origin investing in India is different derivatives such as share, securities, corporate bounds, etc. They may be public/govt. owned or privately owned—mutual funds, pension funds and insurance (life) companies are the major ones in India.

DIRECT COST

The direct material and labour cost of a product–proportionally varies with the total output.

DIRECT INVESTMENT

The expenditure on physical assets (i.e., plant, machinery, etc.).

DIRTY FLOAT

A term of foreign exchange managment when a country manipulates its exchange rate under the floating currency system to take leverage in its external transactions.

DISCOUNT HOUSE

A financial institution specialising in buying and selling of short-term (i.e., less than one year) instruments of the money market.

DISGORGEMENT

Disgorgement is a common term in developed markets across the world, though for most market participants in India it is a new thing. Disgorgement means repayment of illegal gains by wrongdoers. Funds that were received through illegal or unethical business transactions are 'disgorged', or paid back, with interest to those affected by the action. It is for the first time in India that the capital markets regulator, SEBI has passed this order of disgorgement; internationally it is the civil courts that have this mandate along with the markets regulator.

Disgorgement is a 'remedial' civil action, rather than a 'punitive' civil action. In the US, individuals or companies that violate Securities and Exchange Commission regulations are typically required to pay both civil money penalties and disgorgement. Civil money penalties are punitive, while disgo-rgement is about paying back profits made from those actions that violated securities regulations.

Interestingly, disgorgement payments are not only demanded of those who violate securities regulations. In the US, anyone profiting from illegal or unethical activities may be required to disgorge their profits. The money disgorged from the violating parties is used to create a 'Fair Fund'–fund for the benefit of investors who were harmed by the violation.

DISMANTLING OF TEXTILE QUOTA

Until December 31, 2004, global textile trade was largely regulated by the quota system. A textile exporting country (for example, India) could not export a particular textile item to an importing country (say, the Us) beyond a fixed quantity, determined bilaterally. The phase-out of textile quota has removed the non-tariff barrier. The move is expected to drive outsourcing of textiles and apparel manufacturing to low-cost destinations. India is considered the *second largest* beneficiary of quota dismantling after China. It has advantages of having an integrated textile industry right from fibre to fashion. According to government projections, India's textile exports is expected to touch $50 billion mark by 2010.

DISSAVING

The situation of higher current consumption over current disposable income by the households–the difference is met by withdrawals from the past savings (*i.e., decrease in saving*).

DOMINO EFFECT

An economic situation in which one economic event causes a series of similar events to happen one after the other. For example, experts believe that the falling of share indices around the world in early-2008 was a domino effect of the sub-prime crisis faced by the US economy. A similar case is cited from the mid-1996 when all major stock markets crashed around the world due to the domino effect emanating from the South East Asian currency crisis.

DOW-JONES INDEX

The US share price index which monitors and records the share price movements of all compaines listed on the New York Stock Exchange (*with the exception of high-tech companies which are listed on the nasdaq stock exchange*). India has its equivalent in the BSE *Sensex.*

DRUG PRICE CONTROL

Drug price control, as the term suggests, means a mechanism or a policy that ensures that *essential* and *life-saving* medicines are available at reasonable prices. Control over cost of medicines to the consumer exists in one form or the other in most countries. Government's control over drug pricing in India had begun in the wake of the Sino-Indian war, but a structured price control mechanism was only first instituted in 1979 with the issuance of the first Drug Price Control Order (DPCO).

The Drugs Price Control Order, 1995 is an order issued by the Government of India under Section 3 of the Essential Commodities Act, 1955. The Order provides the list of price-controlled drugs, procedures for fixation of prices of drugs, method of implementation of prices fixed by government and penalties for contravention of provisions among other things. For the purpose of implementing provisions of DPCO, powers of the government have been vested in the National Pharmaceutical Pricing Authority. As of now, 74 bulk drugs are under price control and there is no price control on 70 to 75 per cent of the retail pharma market.

Drugs and formulation have been subjected to price control for more than three decades now and the industry's stand is that when price control has been abolished in a large number of industries, it is unfair to stifle the pharmaceutical industry with rigorous price control. While the government has expressed that it wants to provide a stable policy environment to the pharmaceutical industry, it has also said that it will ensure the availability of essential and life-saving drugs at reasonable prices to the public.

DUMPING

Exporting a good at a price lower than its price in the domestic market. To neutralise the effects of dumping the importing country may impose a *surcharge* on such imports which is known as the *anti-dumping duty.*

DUTCH DISEASE

When an increase in one form of net exports drives up a country's exchange rate, it is called the Dutch Disease. Such instances make other exports non-competitive in the world market and impairs the ability of domestic products to compete with imports.

The term originated from the supposed effect of natural gas discoveries on the Netherlands economy.

DUTY DRAWBACK SCHEME

The Duty Drawback Scheme (DDS) is provided by the Government of India as a part of export incentives to make exports competitive. Exporters get refund of the central excise (censat) and custom duties on the inputs they use in manufacturing the exportables. Those who are covered by the Duty Entitlement Passbook Scheme (DEPS) are not covered by it. The rates are announced from time to time.

DUTY ENTITLEMENT PASSBOOK SCHEME

The Duty Entitlement Passbook Scheme (DEPS) is an export incentive scheme of the GoI under which exporters get credit (pre-determined by the Direcor General of Foreign Trade) on the export value which they use in future imports thus neutralising all the taxes. No cash is given (unlike the Duty Drawback Scheme). It has been abolished by the GoI, w.e.f. October 1, 2011 after using it for 14 years – the WTO provisions do not allow member countries to carry such schemes.

E-BUSINESS

Using computers and the Internet to link both the *internal* operations (i.e., transactions and communications between the various departments/divisions of the business firm) and its *external* operations (i.e., all its dealings with the suppliers, customers, etc.).

E-COMMERCE

Method of buying and selling goods and services over the Internet – a kind of direct marketing i.e. without the help of any middle arrangement of sales.

ECONOMIES OF SCALE

The long-run reduction in average/unit cost that occurs as the scale of the firm's output increases. The opposite situation is known as *diseconomiess of scale*.

ECONOMIES OF SCOPE

The long-run reduction in average/unit cost that occurs as the scope (diversification) of the firm's activities increase.

EDGEWORTH BOX

A concept for the purpose of analysing the possible relationships between two individuals or countries. It is done using indifference curve.

The concept was developed by Francis Ysidro Edgeworth (1845–1926) who is also credited for analytical tools of *indifference curves* and *contract curves*.

EFFECTIVE REVENUE DEFICIT

[See Chapter 18, *Public Finance in India*]

ENGEL'S LAW

The law which says that people generally spend a smaller part of their budget on food as their income rises. The idea was suggested by Ernst Engel, a Russian statistician in 1857.

ENVIRONMENTAL ACCOUNTING

The method of accounting which includes the ecological and environmental damages done by the economic activities in monetary terms. Integrated environment and economic (green) accounting attempts at accounting for both socioeconomic performance and its environmental effects and integrates environmental concerns into mainstream economic planning and policies. The *green GDP* of an economy is measured by the same method—experimented in Costa Rica, Mexico, Netherlands, Norway, and Papua New Guinea, among others. Indicative estimates suggest that conventionally measured GDP may exceed GDP adjusted for natural resources depletion and environmental degradation by a range between 1.5 per cent and 10 per cent.

ENVIRONMENTAL AUDIT

Assessment of the environmental impact of a firm/public body through its activities. This is done with an objective to reduce or eliminate the pollution aspect.

ENVIRONMENTAL TAXES

As against the Command and Control approach to managing environment, the Economic or Market Based Instruments (MBIs) approach sends economic signals to the polluters to modify their behaviour. The MBIs used for environmental taxes include pollution charges (emission/affluent & tax/pollution tax), marketable permits, deposit refund system, input taxes/product charges, differential tax rates, user administrative changes and subsidies for pollution abatement, which may be based on both price and quality. India has been already collecting taxes on *water* and *air* via thewater Act and the air Act. due to its experience India is among the chief participant in devising the MBIs in the world.

EQUITY LINKED SAVING SCHEME

Equity linked savings schemes (ELSS) are open-ended, diversified equity schemes offered by mutual funds. They offer tax benefits under the new section 80C introduced in the Finance Bill 2005–06. Till the fiscal year 2004–05, maximum investment of Rs. 10,000 was eligible for tax benefits under the erstwhile Section 88 of the I-Tax Act. Effective April 1, 2005, the investment is included in the overall '1,00,000 limit set by the new Budget.

Besides offering the tax benefits, the scheme invests in shares of frontline companies and offers long-term capital appreciation. This means unlike a guaranteed return by assured return schemes like Public Provident Fund or National Savings Certificate, the investor gets the benefit of the upside (if any) in the equity markets.

Unlike other mutual fund schemes, there is a three-year lock in period for investments made in these schemes. Investors planning to build wealth over the long-term and save on tax can use these schemes.

Returns in these schemes are linked to the fortunes of the stock market. It falls in the high risk and high return category. Over the past one year, these schemes have clocked a return of over 30 per cent. The BSE 200 index rose 7 per cent over the past one year. This indicates that these funds outperformed the broader market. However, past performance is not a guarantee for future growth. Investors should assess their respective risk appetites before investing.

EQUITY SHARE

A security issued by a company to those who contributed capital in its formation shows ownership in the company. The other terms for it are 'stock' or 'common stock'.

Such shares might be issued via public issue, bonus shares, convertible debentures, etc. and may be traded on the stock exchanges.

Such shareholders have a claim on the earnings and assets of the company after all the claims have been paid for. This is why such shareholders are also known as the *residual owners*.

ESCROW ACCOUNT

In simple terms, an 'escrow account' is a *third party account*. It is a separate bank account to hold money which belongs to others and where the money parked will be released only under fulfilment of certain conditions of a contract. The term ***escrow*** is derived from the French term 'escroue' meaning a scrap of paper or roll of parchment, an indicator of the deed that was held by a third party till a transaction is completed.

An escrow account is an *arrangement for safeguarding* the 'seller' against its 'buyer' from the payment risk for the goods or services sold by the former to the latter. This is done by removing the control over cash flows from the hands of the buyer to an independent agent. The independent agent, i.e, the holder of the escrow account would ensure that the appropriation of cash flows is as per the agreed terms and conditions between the transacting parties. Escrow account has become the standard in various transactions and business deals. In India escrow account is widely used in public private partnership projects in infrastructure. RBI has also permitted Banks (Authorised Dealer Category I) to open escrow accounts on behalf of Non-Resident corporates for acquisition / transfer of shares / convertible shares of an Indian company.

ESOPs

Employee Stock Option Plans (ESOPs) is a provision under which a foreign company (i.e., MNC) offers shares to its employees overseas. Till February 2005 in the case of local firms, an MNC needed a permission from the RBI before allotting ESOPs, but since then, it does not need any permission provided the company has a minimum of 15 per cent holding in the Indian arm.

EXPLODING ARMS

A term associated with the mortgage business which became popular after the subprime crisis hit the US financial system in mid-2007. Exploding arms are mortgages with initial low, fixed interest rates which escalate to a high floating rate after a period of two to three years.

EXTERNALITIES

Factors that are not included in the gross income of the economy but have an effect on human welfare. They may be *positive* or *negative*–training personnel is an example of the former while pollution falls in the latter.

FCCB

Foreign Currency Convertible Bond, (FCCB) is an unsecured instrument to raise long-term loan in foreign currency by an Indian company which converts into shares of the company on a predetermined rate. It is counted as the part of external debt. It is a safer route to raise foreign currency requirements of a company.

FEDERAL FUND RATE

The federal fund rate (also popular as *Fed Fund Rate* or *Fed Rate*) is the rate of interest banks charge each other on overnight loans in the USA. The rate is fixed by the US central bank Federal Reserve. This is equivalent to the *Repo rate* of India which is fixed by the RBI.

The Federal Reserve cut the Fed Rate by 0.75 per cent on January 22, 2008 (now the rate stands at 3.5 per cent) to ward off the increased fear of a recession in the US economy which has also generated worldwide free fall of share indices since mid-January 2008. In wake of the sub-prime real estate crisis wrecking havoc on the US economy, the Fed Rate has been cut time and again to counter the possible future recession.

FIDUCIARY ISSUE

Issuance of currency by the government not matched by gold securities, also known as *fiat money*.

FINANCIAL CLOSURE

Financial closure is defined as a stage when all the conditions of a financing agreement are fulfilled prior to the initial availability of funds. It is attained when all the tie ups with banks or financial institutions for funds are made and all the conditions precedent to initial drawing of debt is satisfied.

In a Public Private Partnership (PPP) project, financial closure indicates the commencement of the *Concession Period*—the date on which financial closure is achieved is the appointed date which is deemed to be the date of commencement of concession period. In order to give a uniform interpretation to the term, the RBI has provided a definition for 'Greenfield' projects, financial closure is *"a legally binding commitment of equity holders and debt financiers to provide or mobilise funding for the project. Such funding must account for a significant part of the project cost which should not be less than 90 per cent of the total project cost securing the construction of the facility".*

FINANCIAL STABILITY BOARD (FSB)

The Financial Stability Forum (FSF) was established by the G7 finance ministers and central bank governors in 1999 to promote international financial stability through enhanced information exchange and international cooperation in financial market supervision and surveillance. It decided at its plenary meeting in London on March 2009 to broaden its membership by inviting the new members from the G20 countries, namely, Argentina, Brazil, China, India, Indonesia, Korea, Mexico, Russia, Saudi Arabia, South Africa, and Turkey. the FSF was relaunched as the Financial Stability Board (FSB) on April 2, 2009, in order to mark a change and convey that the FSF in future would play a more prominent role in this direction.

FISCAL DRAG

The restraining effect of the progressive taxation economies feel on their expansion—fall in the total demand in the economy due to people moving from lower to higher tax brackets and the government tax receipts go on increasing. To neutralise this negative impact, governments usually increase personal tax allowances.

FISCAL NEUTRALITY

A stance in policy making by governments when the net effect of taxation and public spending is neutral—neither encouraging nor discouraging the demand. As for example, a *balanced budget* is the same attempt of fiscal policy when the total tax revenue equals the total public expenditure.

FISHER EFFECT

A concept developed by *Irving fisher* (1867–1947) which shows relationship between inflation and the interest rate, expressed by an equation popular as the *fisher equation,* i.e., the nominal interest rate on a loan is the sum of the real interest rate and the rate of inflation expected over the duration of the loan:

$$\mathbf{R = r + F;}$$

where R = nominal interest rate, r = real interest rate and F = rate of annual inflation.

The concept suggests a direct relationship between inflation and nominal interest rates—changes in inflation rates leads to matching changes in nominal interest rates.

The Fisher effect can be seen each time one goes to the bank; the interest rate an investor has on a savings account is really the nominal interest rate. For example, if the nominal interest rate on a savings account is 4 per cent and the expected rate of inflation is 3 per cent, then money in the savings account is really growing at 1 per cent. The smaller the real interest rate the longer it will take for savings deposits to grow substantially when observed from a purchasing power perspective.

FLAG OF CONVENIENCE

Shipping rights in oceans and seas are governed by international treaties. Flag of convenience is a grant of a shipping 'flag' by a member of these treaties to a non-member nation establishing the legality of shipping to the latter (*usually used for illegal activities*).

FORCED SAVING

The enforced reduction of consumption in an economy. It may take place directly when the government increases taxes or indirectly as a consequence of higher inflation—a tool usually utilised by the developing countries to generate extra funds for investment. Also known as *involuntary saving*.

FOB

This is the abbreviation of 'free-on-board'—when in the balance of payment accounting, only the basic prices of exports and imports of goods (including loading costs) are counted. It does not count the 'cost-insurance-freigth' (CiF) charges incurred in transporting the goods from one to another country.

FORM OF A LIFE INSURANCE FIRM

A life insurance company can be a joint-stock or mutual entity. If joint-stock, it has to have some capital, to begin with. A mutual fund company need not have any. Prudential, the second largest life insurance company in the UK was a mutual fund company till a few years ago and had no capital. Standard Life, another big company, was a mutual company till a few months ago. If such big companies could function without any capital till recently, there is no reason why LIC cannot.

The policyholders are the owners of a mutual company and the entire profit goes to them. A significant proportion of the profit goes to shareholders in the case of joint-stock companies. The LIC, owned fully by the Government, is effectively a mutual fund company and it is not surprising, therefore, that pressure is being mounted to privatise it, so that a chosen few could not corner its huge profits.

FORWARD CONTRACT

A transaction contract of commodity on an agreed price which binds the seller and buyer both to pay and deliver the commodity on a future date. The price agreed upon is known as *forward* rate.

One must not confuse this with the term 'future contract' as in it, the term of the contract cannot be decided by the mutual needs of the parties involved (which is possible in a 'forward contract').

FORWARD TRADING

A trading system in certain shares (as allowed by the SEBI in India) in which buyers and sellers are allowed to postpone/defer payment and delivery respectively after paying some charges. If the buyer wants deferment, it is known as *badla* (an Indian term for *contango*) and if the seller goes for deferment of delivery of shares, it is known as *undha badla* (in India, elsewhere it is known as *backwardation*).

FRACTIONAL BANKING

A system of banking in which banks maintain a minimum reserve asset ratio in order to maintain adequate liquidity to meet the customer's cash demands in its everyday business (*the SLR in India is such a provision,*).

FREE GOODS

The goods which are in abundance (*as air and water*) and are not considered as scarce economic goods. As such goods have *zero supply price* and they will be used in large volumes resulting into rising environmental pollution (point should be noted that today air and water may not be considered as the typical free goods, at least the 'pure air' and 'pure water').

FREE TRADE

The international trade among an agreed-upon group of countries without any barriers (such as tariffs, quotas, forex controls, etc.), promoted with the objective of securing international specialisation and an edge in their foreign trade.

FREE PORT

A port that is designated as such is the one where imports are allowed without any duty, provided they are re-exported (i.e., *entrepot*). If the same is correct in the case of an area, it is known as the *free trade zone*.

FRINGE BENEFIT TAX

The fringe benefit tax is an additional tax imposed by the Union government in order to bring under the tax net fringe benefits received by the employees from his employer.

The various categories of employers are defined under the new provision. This includes an individual or a Hindu Undivided Family engaged in a business or profession, a company, a firm, an association of persons, a body of individuals, a local authority and every artificial juridical person. The key point is that even individuals running small businesses are covered and thus would include someone who even employs a single person.

It is very important to note the exact definition of fringe benefits because only those items that get covered here would be included for the purpose of taxation. It means any privilege, service, facility or amenity, directly or indirectly provided by an employer to his employees. It also includes such facilities provided to former employees. Any reimbursement made either directly or indirectly to the employer will also be considered as a fringe benefit. Travelling ticket provided by the employer to the employees and his family members would be a fringe benefit. Even an amount, which is a contribution by the employer to an approved superannuating fund would be called a fringe benefit.

This is not the end of the matter for there is a category called *deemed* fringe benefits which will suffer the same tax effect. These are benefits that are deemed to have been provided if the employer has in the course of business or profession incurred any expenses on or made any payment for a whole host of fringe benefits. These include entertainment, festival celebration, gifts, use of club facilities, provision of hospitality facilities, maintenance of any accommodation in the nature of a guest house, conference, employee welfare, use of health club, sports and similar facilities, sales promotion including publicity; conveyance tour and travel including foreign travel, hotel, boarding and lodging, repair, running and maintenance of motorcars, repair running and maintenance of aircrafts, consumption of fuel other than imnndustrial fuel, use of telephone, scholarship to the children of the employees.

Tax calculation has to follow a specific procedure. First one has to check whether the benefit falls under the head of fringe benefits. Once this is determined a certain percentage of the expense is then taken as the value on which the tax is to be levied. These percentage has been listed in the budget. For example, the amount to be considered is 50 per cent of the expenses for entertainment and 20 per cent for conveyance, tour and travel. On this a rate of 30 per cent (i.e., 30 per cent of 50 per cent in case of entertainment) is applied as a tax.

GALLUP POLL

A method of survey in which a representative sampling of public opinion or public awareness concerning a certain subject/issue is done and on this basis a conclusion is drawn.

The credit of developing this research methodology goes to *George H. Gallup* (1901–84), a US journalist and statistian who in 1935 did set up the *American Institute of Public Opinion.* Through his efforts the method developed between the period 1935–40. In the coming times, the poll technique was immensely used by business houses for their market research and the psephologists for election forecasting, around the world.

GAME THEORY

The analysis of situations involving two or more interacting decision makers (that may be individuals, competing firms, countries, etc.) who have conflicting objectives. It is a technique which uses logical deduction to explore the consequences of various strategies that might be adopted by game players having competing interests.

Game theory is a branch of *Applied Mathematics* that studies strategic interactions between agents–where the agents try maximising their pay off. It gives *formal modelling approach* to social situations in which decision makers interact with other agents. The theory generalises maximisation approaches developed to analyse markets such as supply and demand model.

The field dates back from the 1944 classic *Theory of Games and Economic Behaviour* by John von Neumann and Oskar Morgentern (Princeton University Press, N. Jersy, 1944 & 2004; 60th Anniversary Ed.). Neumann was a mathematician and Morgenstern an economist and this book was based on the former's prior research published in 1928 on the *Theory of Parlour Games* (in German).

The theory has found significant applications in many areas outside economics as usually construed, including formulations of nuclear strategies, ethics, political science, and evolutionary theory.

GDRS

While ADRs are denominated in dollars and traded on US National Stock Exchanges, GDRs can be denominated either in dollars or Euros and are commonly listed on European Stock Exchanges. Investors can cash in on the difference in price between local and foreign markets. Some time back ADRs and GDRs were *fungible* one way i.e. foreign investors could convert their ADRs/GDRs into underlying shares and sell them in the local market. However, they were not permitted to reconvert shares bought on the local exchange into ADRs/GDRs. In 2002, *two-way fungibility* was permitted. Under these rule reissuance of depositary receipts is permitted to the extent to which they have been redeemed into underlying shares and sold in the domestic market.

GIFFEN GOOD

The good for which the demand increases as its price increases, rather than falls (opposite to the *general theory of demand*)—named after Robert Giffen (1837–1910). It applies to the large proportion of the goods belonging to the household budget (as flour, rice, pulses, salt, onion, potato, etc. in India)—an increase in their prices produces a large *negative income effect* completely overcoming the normal substitution effect with, people buying more of the goods.

GINI COEFFICIENT

An inequality indicator in an economy. The coefficient varies from 'zero' to 'one'. A 'zero' Gini coefficient indicates a situation of perfect equality (i.e., every household earning the same level of income) while a 'one' signifies a situation of absolute inequality (i.e., a single household earning the entire income in an economy).

GOLDEN HANDSHAKE

A payment (usually generous) made by a company to its employees for quitting the job prior to their service.

GOLDEN HANDCUFF

A royalty/bonus payment by a company to its staff (usually top ranking) to keep them with the company or to save them from poaching by the other companies.

GOLDEN HELLO

A large sum paid by a company to attract a new staff to its fold.

GOLDEN RULE

A fiscal policy stance which suggests that over the economic cycle, government should borrow only to 'invest' and not to finance the 'current expenditure'. The attempts towards 'balanced budgeting', 'zero-based budgeting' developed under influence of this rule.

GOODHART'S LAW

The idea of goodhart which suggests that attempts by a central bank (as RBI in India) to regulate the level of lending by banks imposing certain controls can be circumvented by the banks searching the alternatives out of the regulatory preview.

GO-GO FUND

The highly speculative mutual funds operating in the USA with the objective of earning high profits out of capital appreciation–adopt risky strategies for the purpose (investing in volatile unproven and small shares, etc.), also called the *performance funds*.

GREATER FOOL THEORY

A theory evolved by the technical analysts of stocks/shares according to which some even buy overvalued stocks with the conviction that they will find a *greater fool* who will buy them at higher prices. This is also popular as *castle-in-the-air theory*.

GREENFIELD INVESTMENT

An investment by a firm in a new manufacturing plant, workshop, office, etc.

GREENFIELD LOCATION

An area consisting of unused or agricultural land (*i.e., 'greenfield'*) developed to set up new industrial plants.

GREEN REVOLUTION & INSTITUTIONS

The support of institutions and the governments of the world did play a very vital role in the success of the Green Revolution all over the world.

The International Maize and wheat Improvement Centre (CIMMYT), Mexico and the International Rice Research Institute (IRRI), Manila were the two institutions in strong partnership with national programmes which developed the miracle varieties of rice and wheat that fuelled the green Revolution around the world.

The Consultative Group on International Agricultural Research (CGIAR), set up in 1971 (in Washington DC under the aegis of the World Bank) played a central role in Green Revolution, supporting the works of the CIMMYT and IRRI. Today, the 16 CGIAR support centres around the world generate new knowledge and farming technology for the agriculture sector. Its research products are "global public goods", freely available to all.

GREENSHOE OPTION

A term associated with the security/share market. This is a clause in the underwriting agreement of an initial public offer (IPO) by a company which allows to sell additional shares (usually 15 per cent) to the public if the demand for shares exceeds the expectation and the share trades above its offering price. It gets its name from the *Green Shoe* company which was the first company to be allowed such an option (in the USA, early 20th century). This is also known as *'over-allotment provision'*.

The company availing this option uses the proceeds (i.e. from the greenshoe option) to prevent any decline in market price of shares below the issue price in the post-listing period (in such cases the aforesaid company uses the money to purchase its own shares from the market—as demand increases, the market price of its shares picks up).

GRESHAM'S LAW

The economic idea that 'bad' money forces 'good' money out of circulation, named after Sir Thomas Gresham, an adviser to Queen Elizabeth I of England. This law does not apply to the economies where paper currencies are in circulation. The economies which circulate metallic coins (gold, silver, copper, etc.) of proportional intrinsic values face such situations when people start hoarding such coins.

GREENSPAN PUT

A financial market terminology named after the former chairman, of the US central bank, Federal Reserve, to mean the helpful way he responded to big declines in the stock market by delivering a cut in interest rates.

GREY MARKET

The 'unofficial' market of the newly issued shares before their formal listing and trading on the stock exchange.

GROWTH RECESSION

An expression coined by economists to describe an economy that is growing at such a slow pace that more jobs are being lost than are being added. The lack of job creation makes it 'feel' as if the economy is in a recession, even though the economy is still advancing. Many economists believe that between 2002 and 2003, the United States' economy was in a growth recession.

In fact, at several points over the past 25 years the US economy is said to have experienced a growth recession. That is, in spite of gains in real GDP, job growth was either non-existent or was being destroyed at a faster rate than new jobs were being added.

3G TECHNOLOGY

3G refers to the third generation of developments in wireless technology. It is a collective term for the new communication procedures, standards, and devices that will improve the speed and quality of services on mobiles. 3G-compatible handsets combine the functionality of a mobile phone with that of a PC and a personal organiser/PDA.

3G divides each call or transmission into little packets of data, marking each one with an individual code to show which connection it belongs to. This is a more efficient way of transmitting data, allowing 3G networks to deliver larger files, like pictures and video, at much faster speeds.

3G devices have greater transmission abilities, both in terms of speed and capacity, than 2G or

2.5G. The International Telecommunications Union (ITU) *defines* 3G as any device that can transmit and receive data at 144Kbps or more. In practice, 3G devices can transfer data at up to 384Kbps.

Besides phone calls, 3G allows fax transmissions, e-mails, including large attachments, while on the move. High-speed internet access allows web browsing and fast downloading of data files, software, image or music files. 3G can be used for video conferencing and some 3G handsets can also function as personal organisers, with electronic diaries, contact lists, and automatic reminders. Most 3G networks offer global roaming.

Japan is the *first* country which introduced 3G on a large commercial scale in 2005. 3G is now also in use in France, Germany, and Austria besides some other countries.

There is no single global 3G standard, but the principal technologies of 3G include:

(i) WCDMA, which has been chosen for 3G mobile phone systems in Europe, Asia, and the US. It first converts raw data into a narrow band digital radio signal and then attaches a marker to each data packet to identify it as belonging to a particular communication.

(ii) Customers who already use CDMA can upgrade to newer models. CDMA 2000 IxEV-DO provides always–on packet data connection like landline-based broadband, for mobile internet use.

(iii) EDGE is the technology that allows existing GSM networks to provide 3G services and allows GSM to transmit data at transmission speeds of up to 384 Kpbs.

GSM operators offering EDGE-based services are already providing some 3G-like services including video on the move. 3G requires spectrum in specified bands and telecom regulator TRAI has identified 450 MHz, 800 MHZ, and 2.1 Ghz as 3G bands. 3G services will be launched in India only after the government announces its spectrum policy and allocates spectrum in the required bands. This is expected by the end of 2008. After that, it will take a minimum of three months for operators to rollout 3G services.

HEDGE FUNDS

These are basically mutual funds (MFs) which invest in various securities in order to contain or hedge risks. They are investment vehicles that take big bets on a wide range of assets and specialise in sophisticated techniques of investment. They are meant to perform well in falling as well as rising markets!

Run by former bankers or traditional investment managers by setting up their own funds, they make a lot of money by charging high fees typically 2 per cent management fees besides 20 per cent of the profits out of the investment. As they are unregulated in most of the economies (for example the USA, India, specially) and risky, they accept investments from wealthy and sophisticated investors.

Hedge funds made news in recent times as some of them were caught out by betting the wrong way on the market movements. Some of them also made huge losses by buying the complex packages of debt that contain many of the US mortgage loans which turned sour. It is believed that 33 per cent of stocks traded on the London Stock Exchange and 20 per cent on the New York Stock Exchange are managed by numerous hedge funds. In the case of India, it is believed that foreign investment in the Indian stocks (which accounted for almost 75 per cent of the total stocks by November 2007) has a heavy share of such funds–the Participatory Notes (PNs) route investment (i.e., 52 per cent of the total foreign investment in shares) is considered as hedge fund investment.

In recent years, there have been several high-profile hedge fund collapses. The Long -Term capital Management (LTCM) of the US failing in 1998 had threatened the very stability of the US financial system—looking at the level in impact the regulators managed a bail out for it to prevent an imminent financial collapse. In 2006, the world saw the collapse of another hedge fund in the US, the *Amaranth* which lost $6.5 billion in a month in the natural gas market (The fund in place of a bail out was closed down by the regulators with the investors losing heavily.)

HERFINDAHL INDEX

This is a measure of the level of seller concentration in a market which takes into account the total number of firms and their relative share in the total market output. Also known as *Herfindahl-Hirschman Index.*

HIDDEN PRICE REDUCTION

A quantitative or qualitative increase of a product by keeping the price unchanged. We see it taking place in the case of many goods in the market selling '20 per cent or 33 per cent extra' at the same prices.

HIDDEN PRICE RISE

A quantitative or qualitative decrease in a product without changing the price.

HIDDEN TAX

Addition of an indirect tax into the price of a good or service without fully informing the consumer as, for example, the magnitude of the excise duty in tobacco and alcoholic products is so high that the taxes are added to the products directly.

HISTORIC COST

The original cost of purchasing an asset such as land, machine etc., which is shown in the balance sheet of a firm under this title with an adjustment for the replacement cost of the asset.

HOARDING

An act of unproductive retention of *money* or *goods.*

HOG CYCLES

The cycles of over and under production of goods. This takes place due to time lag in the production process–this happens in case of agricultural products specially.

IMPOSSIBLE TRINITY

This is a term to show the central bank's dilemma in targeting for stable exchange rate, interest rate and inflation while announcing the credit and monetary policy for the economy. As this task is not only challenging but also not possible, it is called as the 'impossible trinity'.

INDIA'S SOVEREIGN RATING

Presently, India is rated by six international credit rating agencies, namely Standard and Poor's (S&P), Moody's Investor Services, FITCH, Dominion Bond Rating Service (DBRS), the Japanese Credit Rating Agency(JCRA), and the Rating and Investment Information Inc., Tokyo(R&I). Information flow to these credit rating agencies has been streamlined.

INDIFFERENCE CURVE

A curve on the graph showing the alternative combinations of two products, each giving the same utility/satisfaction.

INDUCED INVESTMENT

The part of investment (increase or decrease) which takes place due to a change in the level of national income.

IIFCL

The India Infrastructure Finance company Ltd (IIFCL), a Government of India company set up in 2006 to promote public sector investments and public-private partnerships (PPPs) in all areas of infrastructure *except* the telecommunication.

INFERIOR PRODUCT

The good or service for which the income elasticity of demand is negative (i.e., as income rises, buyers go to purchase less of the product). For such products, a price cut results into lesser demands by the buyers.

INFLATION

For all types of inflation see the chapter with the same title.

INSIDER TRADING

A stock market terminology which means transactions of shares by the persons having access to confidential informations which are not yet public—such persons stand to gain financially out of this knowledge (the person might be an employee, director, etc. of the share issuing company or the merchant bank or the book runner to the issue, etc.). Such kind of trading in stocks is illegal all over the world.

INSOLVENCY

The situation when the liabilities of an individual or a firm to creditors exceeds its assets—inability to pay the liabilities from the assets. Also known as *bankruptcy.*

INVENTORY

The stocks of finished goods, goods under the production process and raw materials held by a firm.

INVISIBLE HAND

A term coined by Adam Smith (in his magnum opus *The wealth of Nations, 1776*) to denote the way in which the market mechanism (i.e., the price system) coordinates the decisions of buyers and sellers without any outside conscious involvement. For him this maximises individual welfare.

IPO

An IPO or initial public offering refers to the issue of shares to the public by the promoters of a company for the first time. The shares may be made available to the investors at face value of the share or with a premium as per the perceived market value of the share by the promoters. The IPO can be in the form of a fixed price portion or book building portion. Some companies offer only demat form of shares, others offer both demat and physical shares.

The performance of an IPO depends on many factors such as the promoter's track record, experience in running the business, risk factors listed in the offer document, nature of industry, government policies associated with the industry performance of that sector in the previous years, and also any available forecasts for the industry for the near future.

I-S SCHEDULE

Here 'I-S' stands for 'investment saving'. This graphic schedule displays the combinations of levels of national income and interest rate where the equilibirium condition for the real economy (investment = savings) holds.

ISLAMIC BANKING

It is banking practiced as per the Islamic principle as prescribed in the *shariah* known as *Fiqh al-Muamalat* (Islamic rules on transaction). The Islamic law prohibits interest on both loans and deposits. Interest is also called *riba* in Islamic discourse. The argument against interest is that money is not a good and profit should be earned on goods and services only not on control of money itself. But Islam does not deny that capital, as a factor of production deserves to be rewarded. It, however, allows the owners of capital a share in a surplus which is *uncertain*.

It operates on the principle of sharing both profits and risks by the borrower as well as the lender. As such the depositor cannot earn a fixed return in the form of interest as happens in conventional banking.

But the banks are permitted to offer incentives such as variable prizes or bonuses in cash or kind on these deposits.

The depositor, who in the conventional banking system is averse to risk is a provider of capital here and equally shares the risks of the bank which lends his funds.

Investment finance is offered by these banks through *Musharka* where a bank participates as a joint venture partner in a project and shares the profits and losses. Investment finance is also offered through *Mudabha* where the banks contribute the finance and the client provides expertise, management, and labour, and the profits are shared in a prearranged proportion while the loss is borne by the bank.

Trade finance is also offered through a number of ways. One way is through *mare up,* where the bank buys an item for a client and the client agrees to repay the bank the amount along with an agreed profit later on. Banks also finance on lines similar to *leasing, hire purchase,* and *sell and buyback. Consumer lending* is without any interest, but the bank covers expenses by levying a service charge. Besides, these banks offer a host of fee-based products like money transfer, bill collections, and foreign exchange trading where the bank's won money is not involved.

Islamic banks have come into being since the early 1970s. There are nearly 30 Islamic banks all over the world from Africa to Europe to Asia and Australia and are regulated even within the conventional banking system. The whole banking system in Iran has moved over to the Islamic system since the early 1980s and even Pakistan is Islamising its banking system.

Many of the European and American Banks are now offering Islamic banking products not only in muslim countries, but also in developed markets such as the United Kingdom. The concept is also catching up in countries like Malaysia and Dubai.

As per the Islamic experts, with growing indebtedness of many governments and with bulk of the borrowing going to servicing of the past debt and payment of huge interests, it could be an alternative to conventional banking as practiced in the rest of the world. Wherever it is practiced, *studies* have shown that the rate of return is often comparable and sometimes even higher than the interest rate offered by conventional banks to depositors.

Though there is no full-fledged Islamic bank, there are many NBF intermediaries in Mumbai and Bangalore operating on Islamic principles. Besides, their presence in the form of co-operatives in various parts of the country has been there even before independence.

The Reserve Bank of India, which regulates the banking sector in India has recently appointed a committee headed by the Chief General Manager to look into the prospects of introducing certain Islamic products and banks in India. What is unique is that the products are structured according to norms prescribed in the *shariah*.

In many countries, these banks do not have the power of issuing cheques. Besides, many banks which operate on a very small-scale, do not have adequate internal control system because of which their accounting is not very transparent and also inadequate information is provided to the regulator. Besides, wherever they co-exist with conventional banking, central bank control of bank interest rates is liable to be circumvented by shifts of funds to the Islamic banks.

ISOCOST LINE

A line on the two-axis graph which shows the combination of factor inputs that can be purchased for the same money.

ISOCOST CURVE

A curve on the graph showing the varying combinations of factors of production (i.e., labour, capital etc.) that can be used to produce a given quantity of a product with a given technology.

J-CURVE EFFECT

The tendency for a country's balance of payments deficit to initially deteriorate following a devaluation of its currency before moving into surplus.

JOBBER

An individual active on the floors of the stock exchanges who buys or sells stocks on his own account. A jobber's profit is known as *jobber's spread*. They are also known as *Taravniwalla* on the Bombay Stock Exchange (BSE).

JUNK BOND

An informal term denoting the financial securities issued by a company/bidder as a means of borrowing to finance a takeover bid. Such securities generally include high-risk, high-interst loans, that is why the term 'junk' is used. It is also known as *mezzanine debt*.

KERB DEALINGS

All the transactions taking place outside the stock exchanges.

KHILJI EFFECT

The rulers of the Delhi sultanate didn't understand formal macroeconomics. But they knew one lesson very clearly—it was important to "signal the government's intent to keep expectations in check". Alauddin Khilji personally inspected markets and it worked—checking prices from rising. Such an effect on market is popular in India as the 'Khilji Effect'.

India saw these time-tested lessons followed by the GoI in 2014–15—Central Ministers publicly stated that matters are under control with sufficient quantity of 'onions' and 'potatoes'. The Government brought these two commodities under the purview of the Essential Commodities Act, too. This did show the 'strong intent' of the government to control prices.

Though, the routine statements claiming that 'prices will rise' often started the inflationary spiral (it was repeatedly done by the then Union Minister of Agriculture).

KLEPTOCRACY

A government which is corrupt and thieving—the politicians and bureaucrats in charge using the powers of the state to earn personal benefits/profits. Russia after the disintegration is condsiered to be a clear-cut example when Mafia-friendly government allotted valuable shares of the government companies when they were privatised.

KONDRATIEFF WAVE

A business cycle of 50 years, named after the Russian economist Nikolai kondratieff (wrote so in his book *The Long Waves in Economic Life,* 1925).

He argued that capitalism was a stable system (the business cycle of 50 years implied it), in contrast to the Marxist view that it was self-destructive and unstable—he died in one of the Stalin's prisons.

LAF

The abbreviated form of the Liquidity Adjustment Facility, is part of a financial policy provided to the banks by the RBI in India. The facility commenced in June 2000 under which the banks operating in India are allowed to park their funds with the RBI for short-term periods (i.e., less than one year which is usually from one day to seven days, in practice), known as the *Reverse Reop.* On such deposits to the RBI, the banks get an interest rate of 6 per cent per annum at present.

LAFFER CURVE

A curve devised by the economist Arthur Laffer in 1974 which links average tax rates to total tax revenue. It suggests that higher tax rates initially increase revenue but after a point further increases in tax rates cause revenue to fall (for instance by discouraging people from working). But it is tough to know whether an economy is on the Laffer curve, as higher taxation breeds evasion of taxes too.

LIAR LOANS

A term associated with the financial world which created news after the US financial system was hit by the subprime crisis in mid-2007.

These are the loans wherein borrowers fraudulently mis-state their incomes often egged on by the lender or broker to the bank. Such frauds have been detected along the entire US mortgage financing chain by September 2007–websites freely advertised that for a nominal fee, they could produce sufficient proof of income by generating bank statements, pay slips, income tax returns, and provide references. Lenders in turn *lied* about the real terms and conditions of the loans to borrowers and lied about the quality of loans sold to investors. The whole gamut of these deeds make such mortgage loans the *'liar loans'.*

LIBOR

The London Interbank Offered Rate (LIBOR) is the interest rate on dollar and other foreign currency deposits at which larger banks are prepared to borrow and lend these currencies in the Eurocurrency market. The rate reflects market conditions for international funds and are widely used by the banks as a basis for determining the interest rates charged on the US dollar and foreign currency loans to the business customers.

LIFE-CYCLE HYPOTHESIS

An idea which states that current consumption is not dependent solely on current disposable income of the consumers but is related to their anticipated lifetime income. This hypothesis has its high applied value in the real life economic management.

LIFE INSURANCE: SOME IMPORTANT TERMS

Endowment Policy

Insurance policies where a lump sum is payable either at the end of the policy term or if the insured dies during the policy tenure, are termed as endowment policies.

Beneficiary

A person or organisation legally entitled to receive benefits.

Term Life Insurance

In most cases, term life insurance refers to a product that provides death benefit protection for a specified period of time, say for 30 years. Benefits are doled out under this scheme only if the insured dies during the term.

Whole Life Insurance

It is a policy that provides insurance coverage for the entire life of the individual for a fixed premium throughout his life insurance, coupled with an investment component. Investments could be made in stocks or bonds that lead to accumulation of cash values. The augmented cash reserves are returned once one decides to surrender the policy.

Universal life insurance was created to provide more flexibility than whole life insurance by allowing the policy owner to shift money between the insurance and saving components of the policy.

Variable Universal Life Insurance Policy

A form of whole life insurance policy, this is a policy for those who weigh high risk threshold. It offers cash values that fluctuate based on the performance of the underlying mutual funds in the investment account. It is this investment of premiums in the equity market that carries with it an element of uncertainty.

Premium

This is the amount that the policy holder pays to the insurance company for the benefits provided under an insurance policy. The frequency of premium payments is opted by the individual. Typical premium modes include monthly, quarterly, semi-annual, and annual.

Annuity

An agreement sold by a life insurance company that provides fixed or variable payments to the policy holder, either immediately or at a future date.

Group Life Insurance

A life insurance policy issued to a group of people, usually through an employer.

Lapse

Defaulting on premium payments leads to the termination of an insurance policy. A lapse notice is sent in writing to the policy holder when the policy has lapsed.

Lump Sum

It refers to the proceeds of the policy that is paid to the beneficiary all at once rather than in installments. Typically, most life insurance policies make lump sum payment settlements.

LIQUIDATION

A process of 'winding up' a joint-stock company as a legal entity.

LIQUID ASSET

The monetary asset that can be used directly as payment.

LIQUIDITY

The extent to which an asset can be quickly and completely converted into currency and coins.

LIQUIDITY PREFERENCE

A term denoting a preference among the people for holding money instead of investing it.

LIQUIDITY TRAP

A situation when the interest rate is so low that people prefer to hold money rather than invest it.

In such situations investors do not go to increase investment even if the interest rates on loans are decreased. J. M. Keynes suggested for increased government expenditure or reduction in taxes to fight such a situation.

L-M SCHEDULE

Here 'L-M' stands for 'liquidity-money'. This is a schedule showing the combinations of levels of national income and interest rates where the equilibrium condition for the monetary economy, L = M, holds.

LOCAL AREA BANK

Announced in the Union Budget 1996–97 to ensure a focussed savings and credit mobilisation by defining the clear boundary of operation, the local Area Bank (LAB) operates to a narrow geographical area of three contiguous districts. The private sector is also allowed entry in the segment.

LOCOMOTIVE PRINICIPLE

The idea that in a situation of worldwide *recession* (see the chapter *Business Cycle*), increase in the total demand in one economy stimulates economic activities in the other economies via foreign trade.

LORENZ CURVE

A graph showing the degree of inequality in income and wealth in a given population or an economy. It is a rigorous way to measure income inequality. In this method (for example), personal incomes in an economy are arranged in increasing order; the cumulative share of total income is then plotted against the cumulative share of the population. The curve's slope is thus proportional to per capita income at each point of the population distribution. In the case of complete equality of income, the lorenz curve will be a straight line and with greater curvature the inequality rises proportionally–the *Gini Coefficient* measures this inequality.

LUMP OF LABOUR FALLACY

The fallacy in economics that there is a 'fixed amount of work' to be done i.e. a lump of labour—this may be shared in different ways to create fewer or more jobs in an economy. An economist, D.F. Schloss in 1891 called it the lump of labour fallacy because in reality, the amount of work to be done is not fixed.

MACRO & MICRO ECONOMICS

In economics, two different ways of looking at the economy have been developed by economists i.e., macroeconomics and microeconomics.

Macroeconomics ('macro' in Greek language means 'large') looks at the behaviour of the economy *as a whole* such as the issues like inflation, rate of unemployment, economic growth, balance of trade, etc. It is the branch of economics which studies the economy in its *total* or *average* term.

Microeconomics (in Greek language 'micro' means 'small') looks on the behaviour of the *units* i.e. the individual, the households, the firms, a *specific* industry, which together make up the economy.

MARGINAL STANDING FACILITY (MSF)

Operationalised on the lines of the existing Liquidity Adjustment Facility (LAF – Repo) in May 2011 under which all Scheduled Commercial Banks can avail overnight funds, up to one per cent of their Net Demand and Time Liabilities (NDTL) outstanding at the end of the second preceding fortnight. The facility is availed at an interest which is 100 basis points above the LAF repo rate, or as decided by the Reserve Bank from time to time. At present it is 9 per cent.

MARGINAL UTILITY

The increase in satisfaction/utility a consumer derives from the use/consumption of one *additional* unit of a product in a particular time period–it goes on decreasing, i.e., the *diminishing marginal utility.*

MARKET CAPITALISATION

A term of security market which shows the market value of a company's share—calculated by multiplying the current price of its share to the total number of shares issued by the company.

MARKET MAKER

An intermediary (may be an individual or a firm) in the secondary market who buys and sells securities/shares simultaneously quoting two-way rates. For example, on the over the counter Stock Exchange of India (OTCEI) only 'market markers' are allowed to operate. The Discount and Finance House of India (SBI DFHI) is the chief market maker in the 'money market' of India.

A market maker plays a very vital role by providing sustainability to liquidity in the secondary market.

MASCS

The Multi-Application Smart Cards (MASCs) system to facilitate simplification of procedures and enhancing the efficiency of Government schemes has been suggested by a Planning Commission Working Group in the context of the Eleventh Five Year Plan. The ***Smart Card*** (i.e., MASCs) has been recognised to be useful in implementation of various Central government schemes like, PDS, Indira Awas Yojana and National Rural Employment Guarantee Scheme (NREGS).

Based on a web-enabled information system the Smart Cards will be based on unique ID, sharing ID, multi-application and access control. The whole system will consist of front, middle, and back end. The electronic card will be the 'front' end of the system which will be the point of delivery where the smart cards will be read and used. The office at 'middle' will be responsible for changing and updating the card periodically (i.e., monthly, quarterly, annually) depending on the type of information and requirement and transfer information from the front end to the back end and vice versa. The office at 'back' end will contain the computerised records, guidelines, accounts and management information systems. The complete digitisation of records will be required by this system.

MARSHALL PLAN

A programme of international aid named after General George Marshall (a US Secretary of State) under which North America contributed around 1 per cent of its GDP in total (between 1948–52) to western Europe to rebuild the economies ravaged in Second World War.

MENU COST

The cost a firm bears in changing the prices of its product—it includes retraining the sales staff, reprinting of the new price list, labelling of goods, and informing the customers about the price change. Higher menu costs discourage the firms going for frequent price changes.

MID-CAP FUNDS

Mutual funds launch sector-specific funds to attract investments. Similarly, they mobilise resources from investors with an objective of investing in mid-cap shares. The Fund Manager chooses the mid-cap shares that can become a part of the portfolio. His job is to outperform the benchmark like the CNX Midcap 200 indexes in terms of the returns. There are thousands of funds world over that focus on investing in medium or small-cap companies.

MFBS

In August 2007, the Reserve Bank of India released a Manual on Financial and Banking Statistics (MFBS), first of its kind, which works as a reference guide and provides a methodological framework for compilation of statistical indicators encompassing various sectors of the economy.

MID-CAP SHARES

There is no classical definition of mid-cap shares. The name 'mid-cap' originates from the term, *medium capitalised*. It is based on the market capitalisation of the stock. Market capitalisation is calculated by multiplying the current stock price with the number of shares outstanding or issued by the company. The definition of mid-cap shares can vary across markets and countries. In case of India, the National Stock Exchange defines the mid-cap universe as stocks whose average six months market capitalisation is between Rs. 75 crore and Rs. 750 crore. In the US, mid-cap shares are those stocks that have a market *capitalisation* of Rs. 9,000 crore to Rs. 45,000 crore. In India, these shares will be classified as *large cap shares*. Thus, classification of shares into large-caps, mid-cap and small-cap is made on the basis of the relative size of market in a country. The total market capitalisation of US markets is $15 trillion. In India, the market capitalisation of listed companies is around $600 billion.

The theory is that large-cap shares have lesser growth potential since the turnover and profits of large companies are already high in the context of that particular market. On the other hand, mid-cap shares are considered an attractive avenue for investing because their growth rate should be faster. It is analogous to investing in an emerging market, like India, as compared to a mature market. However, on the flip side, mid-cap shares are of small companies where revenue and profits could be more volatile than large companies. At the same time, the availability of shares for trading in the secondary market is also limited in comparison to large-cap shares.

The *free float factor*, as it is called, is a key to active trading in shares since investors want an easy entry and exit. Typically, the promoter holding in these companies is high and there is very little public shareholding. Thus, a volatile financial performance and an inadequate free-float make investing in mid-cap shares more risky than big company shares. Moreover, the faster growth argument is obviously a generalisation which may or may not hold for individual companies.

The National Stock Exchange manages an index called CNX Midcap 200. The objective of such an index is to capture the movement in the mid-cap shares segment. According to the NSE, CNX Midcap 200 represents about 77 per cent of the total market capitalisation of the mid-cap universe and 75 per cent of the total trade value. This index provides investors a broad-based benchmark for comparing portfolio returns in the mad-cap segment.

MERCHANT BANKING

A financial world business of providing various financial services other than lending such as public issue management, underwriting such issues, loan syndication management, mergers and acquisition related services, etc.

MEZZANINE FINANCING

Mezzanine financing is defined as a financial instrument which is a *mix* of 'debt and equity' finance. It is a debt capital that gives the lender the rights to convert to an ownership or equity interest in the company. It is listed as an asset on company's balance sheet. As it is treated as equity in a company's balance sheet, it allows the company to access other traditional sources of finance.

In the hierarchy of creditors, mezzanine finance is subordinate to *senior debt* but ranks higher than *equity*. The return on mezzanine finance is higher in relation to debt finance but lower than equity finance. It is also available quickly to the borrower with *little* or *no collateral*. The concept of mezzanine financing is just catching up in India. Mezzanine financing is used mainly for small and medium enterprises, infrastructure and real estate. *ICICI Venture's Mezzanine Fund* was the first fund in India to focus on mezzanine finance opportunities.

MIBID

The Mumbai Inter Bank Bid (MIBID) is the weighted average interest rate at which certain banks in Mumbai are ready to borrow from the call money market.

MIBOR

The Mumbai Inter Bank offer Rate (MIBOR) is the weighted average interest rate at which certain banks/institutions in Mumbai are ready to lend in the call money market.

Middle Class

We keep hearing and reading use the term 'middle class' frequently. But who are the middle classes? There are still no universally accepted criteria for defining the middle class. Simply put, they are neither rich nor poor. Even the income criterion has not been settled. According to the National Council of Applied Economic Research (NCAER), a family with an annual income between Rs. 3.4 lakh and Rs. 17 lakh (at the 2009-10 price levels) falls in the middle class category. According to NCAER, by 2015–16, India will be a country of 53.3 million middle class households or about 267 million people.

Microcredit

Smaller credit/loan to small and needy borrowers who are outside the reach of commercial banks, for the purpose of undertaking productive activities.

Misery Index

An index of economic misery that is sum of the rates of inflation and unemployment for an economy–higher the value greater is the misery.

Monetary Neutrality

The idea that changes in money supply have no effect on real economic variables (such as output, real interest rates, unemployment etc.,) if money supply increases by 10 per cent, for example, the price will increase by the same level.

A core belief of Classical Economics, the idea was put forth by David Hume in the 18th century. Today this is not considered a valid idea.

MONEY ILLUSION

A phrase coined by J. M. Keynes to denote the misleading thinking among people that they are getting richer as a result of inflation when in reality the value of money decreases.

The phrase is used by some economists to argue that a small amount of inflation may not be a bad thing and could even be beneficial as it may help to 'grease the wheels' of the economy—a feeling of getting richer (let it be illusory itself!).

MORAL HAZARD

One among the two kinds of market failure often associated with the insurance sector. It means that the people with insurance cover may take greater risks than the uncovered ones as they know they are protected so the insurer may get more claims it bargained for. the other kind of market failure is the *adverse selections* also related to insurance business.

MOST FAVOURED NATION

As per the WTO agreements, member countries cannot *normally* discriminate between their trading partners. If any country grants one country a special favour such as a lower customs duty rate for one of their products the same would need to be extended to all other WTO members. This principle is known as Most Favoured Nation (MFN) treatment.

MFN is governs trade in ***goods***. MFN is also a priority in the General Agreement on Trade in ***Services*** (GATS) and the Agreement on Trade-Related Aspects of ***Intellectual Property*** Rights (TRIPS). However, there are some *exceptions* under WTO regime which allow mwmber countries to—

(i) Set up a 'free trade agreemen't that applies only to *goods* traded within the group (discriminating against goods from outside).

(ii) Give developing countries special access to their markets.

(iii) Raise barriers against products that are considered to be traded unfairly from specific countries.

(iv) To discriminate, in limited circumstances, in services.

But the agreements only permit these exceptions under strict conditions. In general, MFN means that every time a country lowers a trade barrier or opens up a market, it has to do so for the same goods or services for all its trading partners whether developed or developing.

MULTI-FIBRE ARRANGEMENT (MFA)

Up to the end of the Uruguay Round (1986–94), textile and clothing trade were negotiated bilaterally and governed by the rules of MFA, introduced in 1974. This provided for the application of selective quantitative restrictions (quota) when surges in imports of particular products caused, or threatened to cause, serious damage to the industry of the importing country. The Multi-fibre Arrangement was a major departure from the basic GATT rules and particularly the principles of non-discrimination.

On January 1, 1995 MFA was replaced by the WTO Agreement on Textiles and Clothing (ATC) which sets out a transitional process for the ultimate removal of these quotas in stages. The MFA regime, however, continued till December 31, 2004 until quota was completely phased out.

In the MFA regime, higher quota was allocated to various countries irrespective of cost competitiveness. Apparel exports from countries like Nepal, Bangladesh, Sri Lanka, Taiwan, and other South East Asian nations thrived due to quota protection in the lucrative EU and the US markets. But most of these nations lack competitive edge. Their market share was expected to be grabbed by countries like China and India as they offer cheaper and better products.

The ATC was a transitional instrument meant for progressively integrating textile and clothing products into GATT 1994. It laid down the integration procedure and stipulated how members should integrate textile products into the rules of GATT 1994 over the 10-year period which ended on December 31, 2004. The process was to be carried out progressively in three stages (3, 4, and 3 years) with all textile products being integrated at the end of the 10-year period.

First stage began on January 1, 1995 with the integration by members of products representing not less than 16 per cent of its total 1990 imports of all products under quota. At stage 2, on January 1, 1998, not less than a further 17 per cent was integrated. At stage 3, on January 1, 2002, not less than a further 18 per cent was integrated. Finally at the end, on January 1, 2005, all the remaining products (amounting upto 49 per cent of 1990 imports into a member) stood integrated and the ATC was terminated.

MUTUAL FUNDS

The key consideration while investing in a mutual fund are *safety, liquidity*, and *return*. Safety is assured when investors are able to get back their money. Liquidity enables investors exit the fund any time. There are no assured returns from mutual funds and they vary with the scheme under each fund. The schemes are structured to suit the risk-bearing capacity of unit holders and the nature of deployment of funds by the various schemes.

The structure of mutual funds is governed by the Securities and Exchanges Board of India under the SEBI (Mutual Fund) Regulations 1996. These regulations make it mandatory for mutual funds to have a three-tier structure: a sponsor, a trustee, and an asset management company (AMC). The sponsor is the promoter of the mutual fund and appoints the trustees. The trustees are responsible to the investors in the mutual fund and appoint the AMC for managing the investment portfolio.

The AMC is the business face of the mutual fund, as it manages all the affairs of the mutual fund. The mutual fund and the AMC have to be registered with the SEBI. SEBI regulations also provide for who can be a sponsor, trustee, and AMC, and specify the format of agreements between these entities. These agreements provide for the rights, duties, and obligations of these three entities.

Mutual funds are the preferred route for investors, particularly small and retail investors, who do not have the knowledge or time to directly trade in the equity and debt markets. The funds are managed by qualified investment professionals and other service providers who are paid for their services. Portfolio diversification, professional management, and, reduced risk are among the myriad advantages of mutual funds.

Mutual funds invest in multiple asset classes, enable continuous evaluation and provide higher flexibility in investment plans.

Investors in mutual funds have a wide choice from an assorted variety of funds and schemes with several products on offer. Competition in the industry has led to innovative changes in standard products by fund houses. The product choice enables investors to choose options that suit their return requirement and risk appetite. They can combine the options to arrive at their own mutual fund portfolios that will fit their financial planning objectives. The funds are invested in a portfolio of marketable securities, reflecting the investment objective. The value of the portfolio and investors' holdings alter with change in the market value of investments.

Mutual funds predominantly invest in equity shares and debt instruments. Under *equity funds*, one can invest in diversified equity schemes, primary market schemes, index based funds, and sectoral funds.

Debt funds invest predominantly in debt markets. Diversified debt funds, income funds, gilt funds, liquid and money market funds, fixed term plans, and floating rate funds are among the categories of debt funds. While equity funds suit growth objectives, debt funds fit income objectives.

Mutual fund houses also offer *balanced funds* and *money market funds*. Balanced funds invest in equity and debt in specified proportions while money market funds are preferred by institutional investors which churn their investments depending on the need and view.

NARROW BANKING

Short-term lending in risk-free asset is narrow banking. A suggestion for such banking was given by the committee on Financial System (CFS) in 1991 for the weak banks of India.

NASDAQ

The National Association of Security Dealers Automated Quotation (NASDAQ) is a US stock exchange based in New York which specialises in the high-tech companies' shares. A similar exchange *Techmark* exists in London too. (It is an arm of the London Stock Exchange.)

NASH EQUILIBRIUM

A concept in game theory named after John Nash, a mathematician and Nobel prize winning economist, which occurs when each player is pursuing their best possible strategy in the full knowledge of the strategies of all the other players—once the equilibrium is reached, none of the players has any incentive to change their strategy.

NEO-CLASSICAL ECONOMICS

The school of economics based on the writings of Alfred Marshall (1842–1924) which replaced the classical economics by the 19th century, also known as the *'marginal revolution'*.

NET WORTH

Net worth for a company is its total assets minus total liabilities. This is an important determinant of the value of a company, considering it is composed primarily of all the money that has been invested since its inception, as well as the retained earnings for the duration of its operation. Net worth can be used to determine creditworthiness because it gives a snapshot of the company's investment history. This is also called as *owner's equity, shareholders' equity,* or *net assets.*

In case of an individual, net wroth is the value of a person's assets, including cash, minus all liabilities – the amount by which the individual's assets exceed their liabilities is considered the net worth of that person.

NEW PENSION SCHEME

Pension reforms in India have evolved primarily in response to the need of reform in the Government pension system. This had been designed to make a shift from defined-benefit to defined-contribution by putting a cap on Government's liability towards civil servants' pension. As a result of implementation of the New Pension System (NPS), all employees of the Central Government and Central autonomous bodies, with the exception of the armed forces, are now covered by this defined-contribution scheme with effect from January 1, 2004. Subsequently, 27 State Governments have notified and joined the NPS for their employees. The NPS to was opened to all citizens of India on May 1, 2009, on voluntary basis - the challenge is to spread the message of the NPS and old age income security to people in the unorganized sector across the country.

The pension fund managers manage three separate schemes, consisting of three asset classes, namely (i) equity, (ii) Government securities, and (iii) credit risk-bearing fixed income instruments, with the investment in equity subject to a cap of 50 per cent.

NINJA

A mortgage business terminology became common word after the US subprime crisis of mid-2007 which is an acronym for the borrowers with no income, no job or assets.

NOMINAL VALUE

The value of anything calculated at the current prices. It does not include the effect of inflation during the periods and gives misleading idea of value.

NON-WORKERS

The *Census of India* defines non-workers as the persons who did not 'work at all' during the reference period. They constitute—

(i) Students who did not participate in anyeconomic activity paid or unpaid,

(ii) Household duties who were attending to daily household chores like cooking, cleaning utensils, looking after children, fetching water etc. and are not even helping in the unpaid work in the family farm or cultivation or milching,

(iii) Dependants such as infants or very elderly people not included as *worker*,

(iv) Pensioners drawing pension post-retirement, not engaged in any economic activity.

(v) Beggars, vagrants, prostitutes and persons having unidentified source of income and with unspecified sources of subsistence and not engaged in any economically productive work.

(vi) Others, which includes all Non-workers who may not come under the above categories such as rentiers, persons living on remittances, agricultural or non-agricultural royalty, convicts in jails or inmates of penal, mental or charitable institutions doing no paid or unpaid work and persons who are seeking/available for work.

[Also see entry *'Worker'*]

NORKA

Indians work abroad and *remit* much of their earnings back home. Kerala is a state where non-residents contribute significantly to the state's resources. Keeping this important revenue channel in mind, the Government of Kerala launched the department of Non-resident Keralites' Affairs (NORKA) in 1996 to redress the grievances of Non-Resident Keralites (NRKs). NORKA is the ***first*** of its kind formed by any Indian state.

It makes efforts to solve the grievances raised in petitions for remedial action on threats to the lives and property of those who are left at home, tracing of missing persons abroad, compensation from sponsors, harassment from sponsors, cheating by recruiting agents, educational facilities for children of NRKs, introduction of more flights, assistance to stranded Keralites, etc.

NORKA has established *NORKA Roots* that acts as an interface between the NRKs and the Government of Kerala. Some important *objectives* are creation of a heritage village for parents of non residents, cultural exchange programmes, promotion of Malayalam language, employment mapping, maintaining a data base, etc.

NORMAL GOODS

The goods whose demand increases as income of the people increases. It is just opposite of *inferior goods*.

NULL HYPOTHESIS

An idea that is put to the test. In econometrics, experts start with a null hypothesis (i.e., a particular variable equals a particular number), then crunch the data to verify it in accordance with the laws of *statistical significance*. The chosen null hypothesis is often just opposite to what the experimenter believes.

Statistical significance means that the probability of getting the result by chance is low. It is most commonly used measure is that there must be a 95 per cent chance that the result is right and only 1-in-20 chance of the result occurring randomly.

NUMERAIRE

A monetary unit which is used as the basis for denominating international exchanges in a product and financial settlements on a common basis. For example, the US dollar being used as the numeraire of international oil trade, the Special Drawing Rights (SDRs) as the numeraire of the IMF transactions, etc.

NVS

Non voting Shares (NVS) are the equity shares not having right to vote at the general meetings of the company. But these shares get higher dividend than the shares having voting rights. A company in India may issue such shares maximum to the 25 per cent of the total issued share capital and such shares cannot get more than 20 per cent higher dividend than the shares with voting rights.

OIL BONDS

Over the last few months there have been many reports on India state-owned oil refining companies like IOC, BPCL, and HPCL reeling under the impact of the rise in crude oil prices. These companies have been hit as they are unable to pass on the rise in price to the consumer due to heavy subsidies on some products. With the oil companies being heavily impacted in the first quarter of this financial year, the government has finally agreed to a package, which proposes issuance of special oil bonds.

The oil bonds are special bonds issued by the government to partly compensate state-owned oil companies for not increasing the retail prices of products like LPG and kerosene in line with the rise in crude oil prices.

OKUN'S LAW

Based on the empirical research of *Arthur Okun* (1928–80), the law describes the relationship between unemployment and growth rate in an economy. As per it, if GDP grows at 3 per cent p.a., the unemployment rate would not change. In the case of faster growth rates, every extra above the 3 per cent will have a decrease in the unemployment rate by its half (i.e., a 4 per cent growth rate will decrease unemployment by 0.5 per cent–half of 1 which is the extra above 3 per cent). Similarly, a growth rate below 3 per cent will have the same but opposite impact on unemployment (i.e., increases it).

Though the law was perfectly correct for the period of the US economy Okun studied, it may not be valid today in either US or anywhere else. But in general, the law is still used by experts and policy makers as a rule of thumb to estimate the relationship between growth rate and job creation.

OPEN MARKET OPERATION

An instrument/tool of monetary policy under which sale/purchase of government Treasury Bills and bonds takes place as a means of controlling money supply.

OPPORTUNITY COST

A measure of the economic cost of using scarce resources to produce one particular good or service in terms of the alternative thereby foregone, also known as the *economic cost.*

OUTCOME BUDGET

An outcome budget measures the development outcomes of all government programmes. For instance, it will tell a citizen if money has been allocated for building a primary health centre, whether the centre has indeed come up. In other words, it is a means to develop a linkage between the money spent by a government and the results, which follows. The concept has developed in many democratic systems to make budgets more cost-effective. According to experts, it signals the emergence of an important tool for effective government management and accountability. Earlier too, there have been efforts to bind government expenditure to results, like zero-based budgeting. But experts acknowledge that an outcome orientation is a better means to achieve the same objective. In India, the central government decided that with effect from the fiscal year 2006–07, it will put up in the public domain information about spending by ministries so that all stakeholders, including the people's representative, civil society and the intended beneficiaries of the schemes and projects can scrutinise how well a project has been implemented. This will ensure value for money for government expenditure.

This means, every ministry would have to present its preliminary outcome budgets while proposing its demand for grants to the Ministry of Finance. It is a sort of examination of expenditure before they are made, instead to a post expenditure scrutiny. The Expenditure Finance Committee, for instance, which sanctions government plans of upto Rs. 100 crore, has recently modified its rules and decided to ask of real definition of outcomes at the stage of planning a programme. 'At the end of the year, we should ask not how much has been spent, but what has been achieved,' the Finance Minister has said explaining the rationale for the exercise. Admitting that converting outlays into outcomes is a complex process, which may differ from ministry to ministry and programme to programme. The Finance Minister said administrative ministries have to develop a commitment to make the exercise successful.

In addition, converting outlay into outcomes will require ensuring the flow of right amount of money at the right time to the right level, with neither delays nor 'parking' of funds; effective monitoring and evaluation systems, which indicate the areas requiring further calibration and honing of processes to deliver the intended outcomes; and the involvement of the community or target groups for whom the schemes are meant.

The exercise is a joint effort of the finance ministry and the Planning Commission. The latter gave final shape to the consolidated Outcome Budget of the administrative ministries after detailed discussion with them. The document will also be put up on the web for the people to give their comments.

A new division called the Programme Outcome and Response Monitoring Division has been created within the Planning Commission to co-ordinate the initiative. The Division will try to bring a fair degree of uniformity of approach across the ministries, but with due regard to the special nature of their collective responsibilities, programmes, and projects. This means that while it is relatively easy to find out if the defence ministry has spent its budget to buy a new weapons system, it is far more difficult to establish if Rs. 100 crore spent on a block has helped families to move above the poverty line. So the yardsticks have to take into account such differences.

Some of the common yardsticks to be employed to measure outcome include standardising the unit cost of delivery, bench-marking the standards and quality of outcome, and capacity-building of requisite efficiency at all levels, in terms of equipment, technology, knowledge and skills. Accordingly, implementing agencies will have a clearer idea of what is expected of them, and can be assessed against agreed performance indicators.

OVER THE COUNTER

The financial papers/securities which can be bought or sold through a private dealer or bank rather than on a financial exchange. The term has its use in the non-financial world too–purchasing medicines from a medical store without the doctor's prescription is an over-the-counter deal in drugs.

PARALLEL IMPORTING

A type of arbitrage where an independent importer buys product of a particular supplier at low price in one country and resells it in direct competition with the supplier's distributors in another country where prices are higher.

It promotes free trade and competition by breaking down barriers to international trade and undermines price discrimination between markets covered by the suppliers.

PARETO PRINCIPLE

The maximisation of the economic welfare of the community. Named after the Italian economist Vilfredo Pareto (1843–1923), this points to a situation in which nobody can be made better off without making somebody else worse off.

By an efficient use of resources an economy is able to do so i.e., without making somebody else worse off, somebody might be made better off. In reality, change often produces losers as well as winners. Pareto optimality does not help judge whether this sort of change is economically good or bad.

PARKINSON'S LAW

A proposition by C. Northcote Parkinson which suggests that work expands according to the time available in which it is done.

PENNY STOCKS

Very low-priced shares of small companies which have low market capitalisation. The term made news in mid-2006 when some of the 'penny stocks' did show a high rise in their trading prices in India at the BSE as well as the NSE.

PHILLIPS CURVE

A graphic curve depicting an empirical observation of the relationship between the level of unemployment and the rate of change of money wages and, by inference, the rate of change of prices.

It was in 1958 that an economist from New Zealand, A. W. H. Phillips (1914–75) proposed that there was a trade-off between inflation and unemployment–the lower the unemployment rate, the higher the inflation rate–governments simply need to choose the right balance between the two evils.

PIGGYBACK LOAN

A term associated with mortgage business got popular in the wake of the US subprime crisis mid-2007. Piggyback loan is a second mortgage enabling a borrower to buy a house with little or no equity.

PIGOU EFFECT

Named after Arthur Cecil Pigou (1877–1959), a sort of wealth effect resulting from deflation/disinflation (i.e., price fall) – a fall in price level increases the real value of people's money, making them wealthier inducing increased spending by them; higher demand creation leads to higher employment.

PFRDA

In 2002–03, the government announced its intention to move toward a new pension scheme.

The reason for this change was the growing liabilities of both the Central and state governments on account of pension payments. These liabilities are discharged by the government out of general revenues, instead of a specific dedicated sustainable fund. Recognising the inherent dangers, an interim Pension Fund Regulatory Development Authority (PFRDA) was set up on January 1, 2004. subsequently, the Interim authority was disbanded and an ordinance was promulgumated in late December 2004, followed up with the PFRDA bill in the budget session of Parliament.

The PFRDA will be a regulator on the lines of the watchdogs for insurance and capital market, to regulate and supervise pension funds in the country. It will regulate the new pension scheme which has been in vogue since January 1, 2004 for all fresh entrants to the central government, excusing the armed forces. the PFRDA will also regulate the new pension schemes announced by state governments besides all gratuity and superannuating funds. However, other social security schemes which are in operation now like the one offered by Employees Provident Fund, Coal Miners Provident Fund, Seaman Provident Fund, Assam Tea Provident Fund, to name a few, will be out of the purview of PFRDA as they are governed by specific legislations.

Besides regulation of pension funds, the PFRDA will also have a promotional role to play like other regulators in the country. This will also mean an educational awareness role also. The pension fund regulator will evolve guidelines in consultation with the government on opening up of the pension sector. The PFRDA will also have to curb fraudulent and unfair practices in the sector by participants and protect the interests of subscribers. A pension fund subscriber education and protection fund will also be set up down the line in keeping with its mandate.

The PFRDA will decide on how many pension fund managers ought to be allowed initially, the kind of schemes, the norms for selection of the pension fund managers, capital requirements for these players and the investment norms for the pension funds.

It will also grant licences to pension fund managers. In short, all the operational guidelines for pension fund management will be laid down by the PFRDA. Besides, the regulator will also prescribe the level of investment by the pension fund managers in various types of instruments, whether debt or equity, both in the local and overseas markets.

PREFERENCE SHARES

The shares which bear a stated dividend and carry a priority over equity shares (in matters of dividend and assets) are also known as hybrid securities (since they have the qualities of equity shares as well as bond). Such shares in India cannot have a life over 10 years.

PRICE-EARNING RATIO

A concept used in the share market to equate various stocks–is a ratio found/calculated by dividing market price of a share by the earning per share.

PRIMARY AND SECONDARY MARKET

Primary market refers to buying of shares in an initial public offering. The shares are bought by applying through a share application form. Secondary market refers to transactions where one investor buys shares from another investor at the prevailing market price or at an agreed price. The shares are bought and sold in the secondary market on the stock exchanges. The investors may buy and sell securities on the stock exchanges through stock brokers.

PRIMARY DEALER

Primary dealer (PD) is an intermediary participating in the *primary* auctions of the government securities (i.e., G-See or the Gilt-edge securities or the Gilt) and the Treasury Bills (TBs); through a PD these instruments reach the secondary market.

Primary dealers are allowed participation in the call money market and notice money market. They get liquidity support from RBI via repos or refinance (against the G-Secs.).

PRISONER'S DILEMMA

A popular example in *game theory* which concludes why co-operation is difficult to achieve even if it is mutually beneficial, ultimately making things worse for the parties involved. It is shown giving an example of two prisoners arrested for the same offence held in different cells. Each prisoner has two options, i.e., confess, or say nothing. In this situation there are *three* possible outcomes:

(i) One could confess and agree to testify against the other as a state witness, receiving a light sentence while his fellow prisoner receives a heavy sentence.

(ii) They can both say nothing and may turn out to be lucky getting light sentences or even be let off due to lack of firm evidence.

(iii) They may both confess and get lighter individual sentences than one would have received had he said nothing and the other had testified against him.

The second outcome looks the best for both the prisoners. However, the risk that the other might confess and turn state witness is likely to encourage both to confess, landing both with sentences that they might have avoided had they been able to co-operate by remaining silent.

In reality, firms behave like these prisoners, not setting prices as high as they could do if they only trusted the other firms not to undercut them. Ultimately, the firms are worse off i.e. all firms suffer.

POPULATION TRAP

A situation of population growth rate greater than the achievable economic growth rate. This makes it difficult to alleviate poverty;–government is suggested to implement population control measures.

POVERTY TRAP

A situation where an unemployed getting unemployment allowance is not encouraged to seek work/employment because his/her after-tax earnings as employed is less than the benefits as unemployed, also known as the *unemployment trap*.

PREDATORY PRICING

The pricing policy of a firm with the express purpose of harming rivals or exploiting the consumer. By price-cutting, firstly the rivals are ousted from the market and later the consumers are exploited as monopolistic suppliers by the firm.

PPP

Purchasing power parity (PPP) is a method of calculating the correct/real value of a currency which may be different from the market exchange rate of the currency. Using this method economies may be studied comparatively in a common currency. This is a very popular method handy for the IMF and WB in studying the living standards of people in different economies. The PPP gives a different exchange rate for a currency which may be made the basis for measuring the national income of the economies. It is on this basis that the value of gross national product (GNP) of India becomes the fourth largest in the world (after the US, Japan, and China) though on the basis of market exchange rate of rupee it stands at the *thirteenth rank*.

The concept of the PPP was developed by the great European conservative economist, Gustav Cassel (1866–1944), belonging to Sweden. This concept works on the assumption that markets work on the *law of one price,* i.e., identical goods and services (*in quantity* as well as *quality*) must have the same price in different markets when measured in a common currency. If this is not the case it means that the purchasing power of the two currencies is different.

Let us look at an example. Suppose that sugar is selling $1 in US and Rs. 20 in India a kilo then the PPP-based exchange rate of rupee will be $1 = Rs. 20. This is the way how *The Economist* of London has prepared its 'Big Mac Index' (comparing the Mc Donald's Big Mac burger prices in different economies).

In theory, the value of currencies in terms of their market exchange rate should converge with their value in terms of the PPP in the long run. But that might not happen due to many factors like the fluctuations in inflation; level of money supply; follow-up to the exchange rate regimes (fixed, floating, etc.), and other.

For the calculation of the PPP, a comparable basket of goods and services is selected (a very difficult task) of the identical qualities and quantities. The other difficulty in computing PPP arises out of the flaw in the 'one price theory' i.e., due to transportation cost, local taxes, level of production, etc. The prices of goods and services cannot be the same in different markets (This is correct in theory only, not possible in practice.)

QIP

Qualified Institutional Placement (QIP) is a policy associated with the Indian stock market for raising capital by issuing equity shares. The companies listed on the BSE and the NSE are allowed (since May 2006) to raise capital by issuing equity shares, or any securities other than warrants, which are convertible into or exchangeable with equity shares. The attractive part of the new QIP is that the issuing company does not have to undergo elaborate procedural requirements to raise this capital. These securities have to be issued to Qualified Institutional Buyers on a discretionary basis, with just a 10 per cent reservation for mutual funds.

Q THEORY

As investment theory for firms proposed by the Nobel prize winning (1981) economist James Tobin (1918–2002). He theorised that firms would continue to invest as long as the value of their shares exceeded the replacement cost of their assets–the ratio of the market value of a firm to the net replacement cost of the firm's assets is known as *'Tobin Q'.* If Q is greater than 1, then it should expand the firm by investment as the profit it should expect to make from its assets (reflected by share price) exceeds the cost of the assets.

If Q is less than 1, the firm would be better off by selling its assets which are worth more than shareholders currently expect the firm to earn in profit by retaining them.

RANDOM WALK

When it is impossible to predict the next step. As per the Efficient Market Theory the prices of financial assets (such as shares) follow a random walk–there is no way of knowing the next change in the price. The reason this theory provides is that in an efficient market, all the information that would allow an investor to predict the next price move is already *reflected in the current price.* Such belief has led some economists to conclude that investors cannot outperform the market consistently.

As opposed to this, some economists argue that asset prices are predictable and that markets are not efficient–they follow a *non-random walk* perspective.

REDLINING

The act of not lending to people in certain poor or troubled neighbourhoods shown on the map with a 'red line'. Even if their credit-worthiness has been judged on the basis of other criteria, they are not considered as borrowers by the banks, simply because they live in that area.

RENT

It has two different meanings in economics:

(i) The first is layman i.e. the income accruing from hiring land or other durable goods.

(ii) The second (also known as *economic rent*) is a measure of *market power* i.e. the difference between what a factor of production is paid and how much it would need to be paid to remain in its current use.

For example, a cricket player may be paid Rs. 40,000 a week to play for his team when he would be willing to turn out for only Rs. 10,000, so his economic rent will be Rs. 30,000 a week.

RENT-SEEKING

Spending time and money not on the production of real goods and services, but rather on trying to get the government to change the rules so as to make one's business more profitable.

It is like cutting a bigger slice of the cake rather than making the cake bigger trying to make more money without producing more for customers. The term was coined by the economist Gordon Tullock.

RENT-SEEKING BEHAVIOUR

The behaviour which improves the welfare of someone at the expense of someone else. A protection racket is the most extreme example of it, in which one group (i.e., the protected one) betters itself without creating welfare-enhancing output at all.

REPLACEMENT COST

The cost of replacing an asset (such as machinery, etc.). Opposite to *historic cost* (i.e., the original cost of acquiring an asset), replacement cost adjusts the effects of inflation.

REPO, REVERSE REPO, & BANK RATE

It is a window which enables a bank or a financial institution to borrow money in the *short term*. In the transaction the entity in question sells government securities or bonds to be lender (another bank or institution), with an agreement to buy the securities back after a specified time and price. It is also called a *repurchase* agreement. (In the US, repo has different meaning; it is used to signify the repossession of hypothicated property by a financier).

A *repo* transaction is in the nature of secured borrowing; the difference between the sale and repurchase price is the borrowing cost. It is usually very short term in nature with the market practice being to conclude the sale and repurchase within a time frame of one day, to a fortnight.

When RBI conducts a repo what it does in effect is lend to banks by purchasing securities and selling them back at a predetermined price. When RBI does a *reverse repo,* it borrows from banks by selling them securities and buying them back at a future date. When RBI does reverse repo, it enables banks to park short-term surplus funds; on the other hand, it's a tool for RBI to manage short-term liquidity. RBI pays an interest of 6 per cent to the banks on reverse repo today. The rate serves as a short term interest rate benchmark for banks and other intermediaries. Similarly, RBI makes funds available to banks through repo at 7.75 per cent today.

In India, only select institutions in the financial sector have RBI's permission to enter into repo and reverse repo transactions.

Significantly, on April 28, 2007, RBI, for the first time allowed listed corporates to participate in the repo market as lenders. Thus, a corporate treasurer can choose between a liquid mutual fund and repo to park surplus money in the short term.

Banks have been banned to do repo with brokerage. The ban, still in force was imposed after the '92 stock market scam masterminded by the late Harshad Mehta. Mehta used the repo/reverse repo operation with various banks as a subterfuge to divert funds to the stock market. After the scam, RBI came up with strict guidelines for repo transactions. It also limited the number of players in repo transactions to participants such as banks and primary dealers.

Unlike a general borrowing or lending transactions in the money market, repos are safer as the lender holds government securities (or other special bonds with the repo status) in its own name. Thus, a repo is a *zero-risk* transaction. A repo helps banks to meet their mandatory requirements for investing in government securities (i.e., the SLR). Under the law, banks are required to invest a certain portion of their deposits in government securities. If their holdings are not up to the prescribed level, they face punitive action. So, if a bank needs securities for a short period, it provides the opportunity.

There are two benchmark rates through which RBI influences interest rates in the system. The first is the *bank rate*, the rate at which it lends to banks. The second is the *reverse repo rate*, the rate at which it borrows funds from the banking sector, and repo rate, the rate at which it makes funds available to banks which need it. However, over the years, reverse repo and repo have emerged as the more dynamic indicators of the interest rates. Remember, the reverse repo rate acts as a floor for lending rates in the money market since banks have the option of lending to the Reserve Bank at the reverse repo rate if short-term money market rates fall below that level.

RESIDUAL RISK

What is left after one takes out all the other shared risk exposures to an asset, also known as *alpha* (a).

When one buys an asset one is exposed to a number of risks, many of them not unique to the asset but reflect broader possibilities (such as the future behaviour of stock market, interest rate, inflation or even government policies, etc.). Exposure to this risk can be reduced by diversification.

RETAIL BANKING

A way of doing banking business where the banks emphasise the individual-based lending rather than corporate lending–also known as *high street banking*. Such banking focusses on consumer loans, personal loans, hire-purchase, etc., considered more cumbersome and risky.

RETROCESSION

The term has got *three* different meanings in which it is used—

(i) The purchase of 'reinsurance' by a 'reinsurance company' (as in the case of India, the GIC going for 'reinsurance' on the 'reinsurance' it has provided to other 'insurance companies' operating in India). This limits the risk that a reinsurance company may face, since it has purchased insurance against an 'event' that might affect a company that it had underwritten (reinsured). If a reinsurance company *continues* to purchase insurance it might 'unknowingly' buy back its own risk, which is known as 'spiraling'.

(ii) The 'voluntary' act of returning ceded property by one to another which may be a result of 'request' to have property returned. But, by definition, it is not the result of a 'forced' transaction. Returning of Hong Kong to China by the UK in 1997 is the best such example of the recent times.

(iii) The act of 'differentiating' and 'diversifying' assets by consolidating and then dividing them amongst a number of stakeholders – by doing so the risk involved is 'retroceded' (i.e., cut down or minimised). This is, usually, done by the 'hedge funds' in their day-to-day portfolio management.

REVERSE TAKEOVER

The term is used to mean two different kinds of takeovers:

(i) Takeover of a public company by a private one, and

(ii) takeover of a bigger company by a smaller one.

RESIDUAL UNEMPLOYMENT

Unemployment of those who remained unemployed even in the times of full employment (as for example employing a severely handicapped person may far outweigh the productivity obtained from him).

REVERSE MORTGAGE

A scheme for senior citizens in India announced in the Union Budget 2007–08. Under this scheme, the senior citizens go to mortgage their house owned by them in reverse to a bank and the bank pays them the agreed money either in installments or lumpsum. Guidelines for reverse mortgage announced by the National Housing Bank (NHB) in May 2007 has a provision of maximum period of 15 years for such mortgage. Once the period of mortgage is complete either the house should be vacated or the bank will sell the house at the market price and the loan of the bank will be settled. If the value of the house is more than the loan, the difference is paid to the senior citizens or their heirs. If the heir wants to possess the house, he/she needs to pay the loan.

REVERSE YIELD GAP

An excess of returns on gilt-edged (government) securities above those on equities. This occurs during periods of high inflation because equities provide capital gains to compensate inflation while the gilt-edged securities do not.

REVEALED PREFERENCE

The notion that what one wants is revealed by what one does, not by what one says–actions speak louder than words.

RICARDIAN EQUIVALENCE

An idea which (generated too much controversies) originally suggested by David Ricardo (1772–1823) and more recently by Barro, that government deficits do not affect the overall level of demand in an economy.

This is because tax-payers know that any deficit has to be paid later, and so they increase their savings in anticipation of a higher tax bill in future; thus government attempts to stimulate an economy by increasing public spending or cutting taxes, will be rendered impotent by private sector reaction.

The equivalence can be seen as part of a thread of economic thinking which holds that only decisions about real variables (e.g., consumption and production) matter, and that decisions about financing will, in a perfectly functioning market, never have an effect.

RISK SEEKING

An act whereby investors prefer an investment with an uncertain outcome to one with the same expected returns and certainty that it will deliver them – the act which cannot get enough risk.

RULE OF THUMB

A rough-and-ready decision-making aid that provides an acceptably accurate approximate solution to a problem. Where refined decision-making processes are expensive (in terms of information gathering and processing them), such a method looks justified.

ROUNDING ERROR

The error which comes up due to rounding off the figures in decimals, for example, considering 3.6 as 4 and 3.4 as 3. Such rounding off the data is never going to be mathematically correct.

SALARY

The payment made to employees of an organisation, firm, etc., for the use of labour as a factor of production. It differs from *wage* in the following two ways:

(i) It is not paid on hourly basis (or for the actual number of hours worked by the employee) as wages are paid, and

(ii) It is usually paid on monthly basis whereas wages are paid on daily or weekly basis.

SATISFICING THEORY

A theory which suggests that firms do not want only 'satisfactory' profits but maximum profits as well as other objectives such as sales increase, size increase, etc. might be having equal or greater importance than profits.

SAY'S LAW

Named after the French economist Jean Baptise say (1767–1832), the law proposes that aggregate supply creates its own aggregate demand.

The logic of the law goes like this–the very act of production generates an income (in the form of wages, salaries, profits, etc.) exactly equal to the output which if spent is just sufficient to purchase the whole output produced. Ultimately, it gives an important clue, i.e., in order to reach full-employment level all that is needed is to increase the aggregate supply.

The key assumption behind the law is that the economic system is 'supply-led' and that all income is spent. But in practice, some income 'leaks' into saving, taxation, etc., and there is no auto-guarantee that all income is 'injected' back as spending. This is why others suggest for a 'demand-led' idea of the economic system under which demand creation is attended vigorously.

SECOND-BEST THEORY

The idea was put forward by Richard Lipsey and kelvin Lancaster (1924–99) in 1956 which suggests a way out of the situation when all the assumptions of an economic model are not met. As per the theory, the second-best situation is meeting as many of the assumptions as possible (but it might not give the optimum or the desired results).

SECURITIES TRANSACTION TAX

[See Chapter 17, *Tax Structure in India*]

SEIGNORAGE

A method of generating resource by a government through printing of fresh notes/currency notes. Money printing at higher rate to pay the government expenditures leads to inflation that enables the government to secure extra resources though that is called 'inflation tax' also.

SEQUESTRATION

The process under which a third party (*the sequestrator*) holds a part of the disputed assets till the dispute is settled.

SHARPE RATIO

The idea of William Forsyth Sharpe (Nobel Economist) which checks whether the rewards from an investment justify the risk. For this Sharpe uses past data of rewards and calculates it using standard deviation. This is why the ratio says nothing about the future performance of the investment.

SHORT SELLING

Selling shares without possessing them. After the prices fell to a certain extent the short-seller covers his position by cheaper shares booking the difference in price as profits. It is also known as *bear operation*. Short-sellers, however, could get caught on the wrong foot if the market reverses the downtrend.

SHUTDOWN PRICE

That lower level of the prices for the product of a firm at which the firm decides to close (*shut*) down – as it has become impossible to recover even the short-run variable cost at the price. Many such instances we get in the Euro-American economies during the period of the Great Depression (1929).

SIXTH PAY COMMISSION

Almost after every 10 years, the central government appoints a pay commission to revise the salary structure of about 5.5 million central government employees. The pay commission is not a constitutional body unlike the Finance Commission, and therefore, the government can have a lot of leeway about which part of the report to adopt and in what time frame.

The first pay commission was constituted in May 1946 and it submitted its report in a year. The abysmal level of salary of the average government employee prompted the establishment of the commission. This may seem surprising, but the appointment of the pay commission was seen as a humane measure—a far cry from today. The average salary of the employees, even after making allowance for the lower living standards of the day, ranged around Rs. 30. The second pay panel was set up in August 1957, based on the recommendation of the first commission to set up one after 10 years. It was also necessitated by the Partition and the need to restructure the bureaucracy accordingly. It gave its report exactly after two years. The financial impact of the report was about Rs. 39.6 crore.

The third pay commission, set up in April 1970, gave its report in March 1973. The implementation of its proposals did cost the government Rs. 144 crore. The fourth commission was constituted in June 1983, and gave its report in three phases within four years. The financial hit on the government was Rs. 1,282 crore. It was the fifth pay commission which really set back the government finances severely. Formed in April 1994, the panel report was acted upon by the government from January 1997. The financial impact of the the fifth pay panel was a whopping Rs. 17,000 crore. If one adds the Rs. 25,000 crore that state governments paid up as salary and pension to their staff, the impact on the country becomes clear. According to a World Bank report the impact of the award of the pay commision on the states was simlar to the Balance of Payments crisis that the Centre faced in 1991. The states had to re-write their fiscal acts considerably.

First, the fifth commission did not suggest the steep hike that the United Front government finally acceded to. It had broadly recommended a 20 per cent rise in salary scale. But the staff unions managed to push it up to 40 per cent from the existing levels.

Recognising the possible fiscal impact of another pay commission, the fifth commission recommended some far-reaching changes in finances. One of the first was a sustained drive to reduce the number of government staff pruning the size of the bureaucracy by at least 30 per cent. It had also asked for introducing a productivity-linked salary structure and other reforms. None of these had been implemented.

However, the carrots have all been implemented. The panel had suggested that for every 100 points rise in DA, the government should merge 50 per cent of the DA with the salaries to revise the pay scales. This was meant to delay the need for another commission but that has not happened.

The best bet against any profligacy by the new commission is the memory of the impact of the last pay commission. The states and Centre have become wiser. So it is on the cards, that there will be no shock like the last time. But just as the last commision led to the enactment of the Fiscal Responsibility and Budget Management Act, the present could result in scuttling of the act, or at least delaying the goals of achieving a 3 per cent fiscal deficit at the Centre and zero revenue deficit by 2009, by another few years. The proposed commision is, however, in a good position to look at the still rising numbers in the government staff rolls and suggest clear cut policy to check it.

SKIMMING PRICE

A pricing method of charging high profits—adopted by a firm when consumers are not price-sensitive and demand is price-inelastic.

SOCIAL COSTS

The costs borne by the society at large resulting from the economic activities by the firms–pollution being a prominent example.

SOLVENCY MARGIN

The term made news in the 1970s concerning a life insurance company. The only requirement, till then, by a life insurance company was that the value of its assets should not be less than the value of its liabilities. The regulators in many conntries felt that the value of assets should exceed the value of liabilities by a certain margin. This margin which came to be known as *'solvency margin'* became a useful device to force shareholder of a life insurance company either to keep in reserve a certain portion of the profit or to bring in additional capital if there is not sufficient profit to meet unforeseen contigencies. The European Union developed an empirical formula taking recourse to the past experience to determine the quantum of margin required. The IRDA has stipulated that the excess of assets (including capital) over liabilities should not be less than 150 per cent of the solvency margin arrived at by the EU formula.

On March 31, 2006, the total liability of LIC stood at Rs. 4,52,000 crore and its assets valued at Rs. 4,52,000 crore, having a comfortable margin that did not require capital infusion (though the IRDA has suggested to raise its capital by Rs. 7000 crore by 2009).

SOVEREIGN RISK

The risk of a government defaulting on its debt or a loan guaranteed by it (all international loans by the private companies are basically guaranteed by the government of an economy).

SPOT PRICE

The price quoted for anything in a transaction where the payment and delivery is to be done now.

SPREAD

A frequently used term of financial market which is the difference between two items, for example, the spread (i.e., the difference) an underwriter pays for an issue of bonds from a company and the price it charges from the public. Similarly, the returns on two different bonds if they are different; the difference is known as the spread.

STANDARD DEVIATION

It is a statistical technique to measure how far a variable moves over time away from its mean (average) value.

STATES' MARKET BORROWING

The state governments, for years, had few worries when it came to raising money from the market as it was done at the tutelage of the centre. However, with the onset of financial sector reforms, the contours of raising funds from the market both for the states and the Centre have changed. In the early days after the central bank had come into existence, Madras had objected to the Reserve Bank of India being given the mandate to manage public debt for states. State loans used to be underwritten then.

However, that practice was stopped in the 1950s. Since then, major reforms have taken place. Starting from the 1990s, increasingly states as well as the Centre have accessed funds at market-related rates. Now increasingly, the onus will be on the states to manage their borrowing programmes adroitly.

The borrowing requirements of states were decided earlier in consultation with the Planning Commission and the finance ministry. The Reserve Bank of India as the banker to states as well as the debt manager handles the floatations. For decades, the borrowings of states or state loans or *tap issues* as they are called used to be on the basis of pre-determined rates. In effect, all states were treated on the same footing when it came to borrowing. Now a part of market borrowings is through the auctions where the rate is determined based on market response with the rest being through the fixed coupon basis.

The Reserve Bank of India used to take into account the borrowing programme of the Central government, liquidity conditions, the cash flow needs of states, future repayment schedules while working out the borrowing programme for states.

A significant change was signalled when the Twelfth Finance Commission recommended the delinking of grants and loans in Plan assistance to states as part of reforms on the borrowing programme front. Earlier, there was a ratio of 70:30 between loans and grants for extending plan assistance to states.

What this meant was that states could access loans from the Central Government for their plan expenditure. These loans were for long tenures of over 20 years and a relatively higher interest spread.

The government has accepted the Finance Commission's recommendations on doing away with such loans. This would mean greater recourse to the markets by states. Now like the Centre, states will have to decide their annual borrowing programme within the framework of their fiscal responsibility programmes. This is expected to help in fiscal discipline.

The Commission and the RBI want to impose some sort of discipline on states on their debt management. If more market borrowings by states governments are carried out through the auction route, it would mean that well-managed states would stand to gain. They would be in a position to obtain better rates as the market would factor in the fiscal strengths of a particular state when pricing is determined.

When states take a recourse to market borrowings through the auction route, there would be greater price discovery besides enhanced secondary market liquidity for such securities.

A state whose credit rating is strong will get a better rate while borrowing while a weaker state may have to settle for a higher rate. This is expected to lead to greater attention and focus fiscal responsibility and debt management by states especially as they cannot look to the Central Government for loans as in the past. The Reserve Bank of India, which is the debt manager for both the Centre and states, wants to progressively raise the share of market borrowings by states under the auction route so that the entire programme is covered through auctions.

STEALTH TAX

A popular name given to an obscure tax increase as for example stamp duty, property tax etc. Which get implemented months later by the time they usually fade out from the public memory.

STOCHASTIC PROCESS

It is a process that shows random behaviour. As for example, *Brownian* motion which is often used to describe changes in share prices by the experts in an efficient market (random walk), is such a process.

SUB-PRIME CRISIS

The word 'sub-prime' refers to borrowers who do not have sound track record of repayment of loans (*it means such borrowers are not 'prime' thus they could be called as 'less than prime' i.e. 'sub-prime'). The* 'sub-prime crisis' which has been echoing time and again recently has its origin in the United States housing market by Late 2007—being considered as the major financial crisis of the new millenium.

Basically, last few years have seen a gradual softening of international interest rates, relatively easier liquidity conditions across the world motivating the investor (i.e., banks, financial institutions, etc.) to expand their presence in the sub-prime market, too. The risks inherent in sub-prime loans were sliced into different components and packed into a host of securities, referred to as asset-backed securities and *collaterised debt obligations* (CDOs). Credit rating agencies have assigned risk ranks (e.g., AAA, BBB, etc.) to them to facilitate their marketability. Because of the complex nature of these new products, intermediaries (such as hedge funds, pension funds, banks, etc.) who held them in their portfolio or through special purpose vehicle (SPVs), were not fully aware of the risks involved. When interest rates rose leading to defaults in the housing sector, the value of the underlying loans declined along with the price of these products. As a result institutions were saddled with illiquid and value-eroded instruments, leading to liquidity crunch. This crisis of the capital market subsequently spread to money market as well.

The policy response in the US and the Euro area has been to address the issue of enhancing liquidity as well as to restore the faith in the financial system. The sub-prime crisis has also impacted the emerging economies, depending on their exposure to the sub-prime and related assets.

India has remained relatively insulated from this crisis. The banks and financial institutions in India do not have marked exposure to the sub-prime and related assets in matured markets. Further, India's gradual approach to the financial sector reforms process, with the building of appropriate safeguards to ensure stability, has played a positive role in keeping India immune from such shocks.

SUBSIDIES

Are subsidies negative taxes? Are they converse of indirect taxes? What are subsidies and why are they important? These are some questions which always make rounds every time the Union Budgets are presented. *Subsidies include all grants on current account made by the government to depress the price of any good or service below its economic cost.* Often subsidies are grants made by public authorities to government enterprises in compensation of operating losses when these losses are clearly the consequences of the policy of the government to maintain prices at a level below costs of production. The regime of subsidies is, therefore, a *political economic policy* framework typical of welfare states (India is one). Various subsidy regimes are meant to ensure distributive justice. Subsidies are directed at various sections of society to assist them economically. In India, the main beneficiaries have been farmers, needy people and those using various forms of public services, social services and economic services. The first includes fiscal and administrative services like justice, jails and police, which are in the nature of pure public goods. The last two categories include a range of goods and services, which are not purely public and where the users identifiable and user charges can be levied. For example, roads and power. Governments make such goods and services available to users at costs lower than what was expended to produce and/or provide them because social benefits of doing so exceed the aggregate of private benefits to individual consumers. For instance, compulsory and free elementary education, a subsidy provided by the government, aids the social development and uplift of the poor and socially depressed classed by making such education easily accessible to them. Subsidies are financed either from tax or non-tax revenue, or result in a deficit.

Broadly speaking and purely at the level of the central government, there are three major types of subsidies–food subsidies (for farmers and the poor who avail the public distribution system), fertiliser subsidies (for farmers), and petroleum subsidies (for the poor and the middle class, on kerosene and LPG, which they directly consume; or diesel which fuels the transport industry that carries essential goods and thus has an impact on their prices). These are clearly visible in the government's budget document. Apart from these, there are also *minor subsidies* such as on interest rates and subsidies hidden in the provision of social and economic services, mainly healthcare and education. In social services, the Centre's participation is limited. Most of the social sector expenditure pertains either to the Union Territories that figure in the Union budget, or are in the nature of departmental transfers to state governments.

The regime of subsidies has been a contentious issue of higher order in India. The benefits from subsidies can be maximised only when they are transparent, well targeted, and suitably designed for effective implementation without any leakages. Various studies have shown how the proliferation of subsidies in India is an outcome of undue expansion of government activities in the provision of goods and services that are not pure public goods. Subsidies result from the government's inability to recover its costs adequately in many of these activities. Critics have blamed this on the ill-considered use of subsidies by political parties for electoral ends and have been arguing for reduction of some subsidies and the phasing out of others. Those who support the continuing of subsidies, however, argue that the focus on reducing subsidies only comes about because of the government's failure to raise tax revenues.

SUBSIDY BIDDING

It is competitive bidding for subsidies, where companies bid against one another to serve an area at the lowest price—the lure is the subsidy and other benefits. This system is a way of administrating subsidies without leaving any room for some competitors or technologies gaining an edge over others. But competitive bidding has anticompetitive effects, since it gives a special advantage to one company. Regulators should adopt a consumer choice system, under which any subsidy for each high cost customer it served. If the customer moved to a competing carrier, the subsidy would move, too.

SUBSTITUTION EFFECT

The replacement of one product for another resulting from a change in their relative prices.

SUNK COSTS

The costs in commercial activities that have been incurred and cannot be reversed. The cost on advertisement, research and development, etc. are examples of such costs. Sunk costs are a big deterrant to new entrants in the commercial world as after the venture has failed these costs cannot be recovered—there is no two-way process here.

SWAP

The act of exchanging one by another. It could be of many economic items:

Currency Swap

The simultanous buying and selling of foreign currencies could be *spot* or *forward/future* currency swaps. This is used by MNCs to minimise the risk of losses arising from exchange rate changes.

Debt swap

Exchanging one debt by another for a fresh term of repayment schedule at the same or usually lower interest rates.

Interest Rate Swap

Exchanging one debt of a particular interest rate for another at lower interest rate.

Product Swap

Exchanging one product for the other as wheat for milk (similar to barter).

SWFs

Sovereign wealth funds (SWFs) are the foreign currency funds held by the governments of the world, specially in Asia and West Asia. After the process of globalisation, freer capital movements to the developing economies had brought enough foreign currencies to some economies. Earlier, such funds used to originate in Singapore and Norway but now we see china, Russia, and the Middle East emerging as the new SWFs economies.

Such funds, estimated to be sitting on a total of $25 trillion, are eagerly looking to diversify into higher yielding riskier assets. Any fast growing economy with open and liberal attitudes to foreign investments with opportunities for investment may face up the inflow of such funds. India is one fit candidate today.

Such funds need to be studied and alllowed entry cautiously as they bring in non-market and extraneous factors with them too, having potential diplomatic, strategic and sovereign dangers to the host economies. In November 2007, the National Security Advisor of India voiced apprehension about such funds.

SWISS FORMULA

Tariff cut formulae are either linear or non-linear. A Swiss formula is a non-linear formula. In a linear formula, tariffs are reduced by the same percentage irrespective of how high the initial tariff is. As opposed to a linear formula, in a non-linear formula, tariff cuts are directly or inversely proportional to the initial tariff rate.

In the Swiss formula, tariff cuts are proportionally higher for tariffs which are initially higher. For instance, a country which has an initial tariff of 30 per cent on a product will have to undertake proportionally higher cuts than a country which has an initial tariff of 20 per cent on the same product.

In the on-going multilateral trade negotiations at the World Trade Organisation (WTO), it has been decided by all participating countries to use the Swiss formula for reducing import tariffs on industrial goods. After a long-standing debate on the number of reduction coefficients to be used in the formula, a unanimous decision was recently taken that there would be two sets of coefficients—one for the developed countries and another for developing countries. A decision on the value of the coefficient is yet to be taken.

India's average tariffs are much higher than those existing in the developed countries. If a linear formula for tariff reduction was used, then its reduction burden would have been proportional to that of developed countries. However, using a Swiss formula could lead India to taking on a greater reduction commitment than its developed counterparts with lower initial tariffs.

India agreed to a Swiss formula because it was decided that developing countries would be allowed to have a higher reduction coefficient than developed countries which could lower their tariff reduction obligations.

A reduction coefficient is part of the Swiss formula. It has a very important role to play in deciding the final reduction commitment. If all other variables in the Swiss formula remain unchanged, then a higher reduction coefficient could lead to lower reduction commitment and vice versa.

India wants that the reduction coefficient for developing countries should be much higher than the coefficient for developed countries. The difference should be enough to negate the effect of the original Swiss formula which weighs in favour of developed countries with lower initial tariffs. It has proposed that a difference between the coefficients should be at least 25 points to ensure that the reduction burden on developing countries is not higher than that on developed countries.

SYSTEMIC RISK

The risk of damage to the health of the whole financial system. In modern financial world, the collapse of one bank could bring down the whole financial system.

TAKEOVER

The process of one firm acquiring the other, also known as *acquisition*. As opposed to the merger which is an outcome of 'mutual agreement', takeovers are 'hostile' moves.

Takeovers may be classified into three broad categories:

(i) *Horizontal takeovers* involve firms which are direct competitors in the same market;
(ii) *Vertical takeovers* involve the firms having supplier-customer relationship; and
(iii) *Conglomerate takeovers* involve the firms operating in unrelated markets but intend diversification.

TAKEOVER BID

An attempt of acquiring the majority share in a firm by another firm. There are various *terms* to show the *'tactics'* applied in such bids either by the bidder or the bidded firms:

BLACK KNIGHT

The launch of an unwelcome takeover bid (as the Mittal's for the Arcelor in recent past).

Golden Parachute

A generous severance term written into the employment contracts of the directors (of a firm) which makes it expensive to sack them if the firm is taken over.

Green Mail

A situation of takeover bid when the bought-up shares by a potential bidder is actually being bought by the directors of the firm itself.

Leveraged Bid

A takeover bid being financed primarily by the loan.

Pac-man Defence

A situation when the firm being bidded for takeover, bids for the bidder firm itself–also known as *reverse takeover bid.*

Poison Pill

A tactic used by the firm being bidded of merging with some other firm in order to make itself less attractive (financially or structurally) to the potential bidder.

Porcupine

Any agreements between the firm being bidded and its suppliers, creditors, etc., which are so complex that after the takeover the bidder firm feels diffculties integrating it.

Shark Repellants

The measures specially designed to discourage takeover bidders (e.g., altering the firm's articles of association to increase the proportion of shareholder votes needed to approve the bid above the usual 50 per cent level, etc.).

White Knight

The intervention of a third firm in a takeover bid which either merges or takes over the victim firm to rescue it from the unwelcome bidder.

TECHNOLOGICAL UNEMPLOYMENT

Unemployment which results from the automation of the production activities (*i.e., machines replacing men*).

THIRD-PARTY INSURANCE

Motor third-party insurance or third-party insurance is a statutory requirement under the Motor vehicle Act in India–also known as *'act only'* cover. A person purchasing a motor vehicle has to go for this compulsory insurance which benefits the third person (i.e. neither the vehicle owner nor the insurance company)–the person who becomes victim of an accident by the vehicle.

Till December 31, 2005, the premium for the insurance was fixed by the Tariff Advisory Committee (an arm of the IRDA) but since then it has been done away with. However, IRDA still continues to fix the premium for the mandatory third-party insurance, though the insurance companies have the freedom to decide on prices for comprehensive cover.

The amount of compensation is largely decided by the earning capacity of the accident victim.

THIRD WAY

An economic philosophy (better say rhetoric) which propagates it is neither capitalism nor socialism but a third (pragmatic) way.

The idea was popularised in the late 20th century by some political leaders having leftist leanings, including bill clinton and Tony Blair. Though it has been hard to pin down it was earlier used to describe the economic model of Sweden.

TIGHT MONEY

When money has become difficult to mobilise, the term is used to show the 'dear money' when the rates of interest run comparatively on the higher side.

TILL MONEY

The notes and coins the commercial banks keep to meet everyday cash requirements of their customers (this is counted as part of their CRR).

TOBIN TAX

A prosposal of imposing small tax on all foreign exchange transactions with the obejctive to discourage destabilising speculation and volatility in the foreign exchange markets.

Proposed by the Nobel prize-winning economist James Tobin (1918–2002), the tax has never been implemented anywhere in the world so far.

TOTAL PRODUCT

The main/core product supported by many peripheral products/services, as for example a car, coming with loan facility, warranties, insurance, and after sale service, etc.

TRADE CREATION

The increase in international trade that results from the elimination or reduction of trade barriers (such as quota, customs, etc.).

TRAGEDY OF THE COMMONS

Refers to the dangers of over-exploitation of resources due to lack of property rights over them ('commons' are the resources neither owned privately nor by the state but are open for free use by all). A rationing or imposing of levy on such resources as a check.

The concept was proposed by a 19th century amateur mathematician william Forster Lloyd.

TRANSFER PAYMENTS

The expenditure by the government for which it receives no goods or services. For example, the expenditures on tax collection, social sector, unemployment allowance, etc.

As such expenditures are not done against any products they are not counted in the national income of the economy.

TRANSFER EARNINGS

The return that an asset must earn to prevent its transfer to the next best alternative use. Any earning above the transfer earnings is known as its *'economic rent'*.

TRANSFER PRICE

A term of international economics via which an MNC charges lesser prices for its exportables to its arm in another economy where tax rates are high, for increasing income. The East India Company did it heavily in pre-independent India.

ULIPS & MFS

Unit linked insurance policies (ULIPs) offer insurance plus investment objective to those who want a higher amount of insurance cover at a marginally higher cost. However, unlike mutual funds, which may be a short-term investment play, ULIPs meet long-term investment objectives. Essentially, ULIPs must be treated as long-term (15-plus years) investment vehicles.

Returns are varied across the risk class. One can categorise risks into three classes for both MF and ULIP schemes—high, medium, and low risks. High-risk policies have a higher exposure to equities and low-risk policies might have low or no exposure to equities. For MFs, high-risk comparable products are diversified equity funds, medium-risks are balanced funds, and low risks are debt instruments.

UNDERWRITING

The process of acceptance by a financial institution of the financial risks of a transaction for a fee. For example, merchant banks underwrite new share issues, guaranteeing to buy up the shares not sold in a public offer (i.e., in the situations of under-subscription).

USURY

Charging an exorbitant rate of interest or even charging interest. Decried by many ancient philosophers and many religions, today most modern economies have some law regulating the upper limit of the interest rates and they consider interest as a reward to the lender for the lending risk.

VEBLEN EFFECT

Named after the American economist Thorstein Bunde Veblen (1857–1929), this is a theory of consumption which suggests that consumers may have an 'upward-sloping demand curve' as opposed to a 'downward-sloping demand curve' because they practice conspicuous consumption (*a downward - sloping demand curve means that the quantity demanded varies inversely to the price i.e. demand falls with price rise*). The concept suggests that quantity demanded of a particular good varies directly with a change in price (*i.e., as price increases, demand increases*).

VELOCITY OF CIRCULATION

A measure of the average number of times each unit of money is used, to purchase the final goods and services produced in an economy in a year.

VENTURE CAPITAL

Generally, a private equity capital which lends capital to the entrepreneurs who are innovative and cannot get the required fund from the conventional set-up of the lending mechanism.

In India, it was the Government of India which did set up the first such fund in 1998–the IVCF.

VULTURE FUNDS

Vulture funds are privately owned financial firms which buy up sovereign debt issued by poor countries at a fraction of its value, then file lawsuits (sue) against the countries in courts, usually in London, New York, or paris, for their full face value plus interest.

A paper prepared for IMF/WB (October 18, 2007) showed that there are now \$1.8b lawsuits against poor countries where people typically live below \$1 a day; 24 countries that have received debt cancellation under Heavily Indebted Poor Countries (HIPCs)initiative, 11 have been targeted by such creditors (i.e., the VFs) and they has been awarded just under \$1b.–money which have gone for schools and hospitals; they are neutralising the good deeds of WB/IMF. As per the IMF, the litigating creditors were concentrated in the US, UK as well as the British Virgin Islands (BVI)—the UK protectorate tax haven. Bush is being pressed by a motion signed by 110 MPs to change the law which allows them to file cases in US courts—VFs contradict US foreign policy.

VOSTRO ACCOUNT

Vostro is an account that one party holds for another. With a view to give more operational leeway, the RBI decided to dispense with the requirement of prior approval of the RBI for opening and maintaining each rupee **vostro account** in India of non-resident exchange houses in connection with the rupee drawing arrangements (RDAs) that banks enter into with them. The approved dealer banks could now take its permission the first time they entered into such an arrangement with non-resident exchange houses from the Gulf countries, Hong Kong, Singapore and Malaysia. Subsequently, they may enter into RDAs, and inform the RBI immediately.

WALRAS'S LAW

The idea that the total value of goods demanded in an economy is always identically equal to the total value of goods supplied.

This could be only correct in a barter economy not in an economy which uses currency as the mode of exchange.

WASTING ASSET

The natural resource which has a finite but indeterminate life span depending upon the rate of depletion (such as coal, oil, etc.).

WEIGHTLESS ECONOMY

The situation of an economy when the output is increasingly produced from intellectual capital rather than physical materials–a shift in production from iron and steel, heavy machines, etc. to microprocessors, fibre optics and transistors, etc. This is the weightless economy, i.e., the *new economy* which arrived in the US (specially) by the end of the 20th century.

WELFARE ECONOMICS

The branch of economics which is concerned with the way economic activity ought to be organised so as to maximise economic welfare. The idea applies to the welfare of individuals as well as countries.

This is normative economics, i.e., it is based on value judgements. It is also called *'economics with a heart'*. This focuses on questions about *equity* as well as *efficiency*.

It employs value judgements about what *ought* to be produced, how production *should* be organised, the way income and wealth *ought* to be distributed, both in present times and in future. As different individuals in different communities have unique set of value judgements (guided by their attitutdes, religion, philosophy, and politics) it has been difficult for the economists to reach a consensual idea upon which they could advise the governments in policy making, known as the *welfare criteria*. Economists and philosophers have been suggesting their brands of the *welfare criteria* since long–Vilfredo Pareto, Nicholas Kaldor, John Hicks, Scitovsky, Amartya Sen, as the few famous ones.

WILDCAT STRIKE

A strike called on by a group of employees without the support of their organised trade union.

WILLIAMSON TRADE-OFF MODEL

A model for evaluating the possible benefits and detriments of a proposed merger that could be used in the application of a discretionary competition policy. The model was developed by Oliver Williamson.

WINNER'S CURSE

The possibility that the winning bidder in an auction will pay too much for an asset since the highest bidder places a higher value on the asset than all other bidders.

WITHHOLDING TAX

A tax imposed on the income on a foreign portfolio (investments). This tax is imposed to discourage foreign investments, to encourage domestic investment, and to raise money for the government.

WORKER (CENSUS DEFINITION)

The *first* definition of 'worker' by *Census* was given in 1872. Over time the term 'work' and 'worker' as defined by ***Census of India*** have undergone several amendments to suit the changing dimensions of work. 'Work' is defined as participation in any *economically productive activity* with or without compensation, wages or profit. Such participation may be physical and/or mental in nature. Work involves not only actual work but also includes –

(i) Effective supervision and direction of work;

(ii) Part time help or unpaid work on farm, family enterprise or in any other economic activity; and

(iii) Cultivation or milk production even solely for domestic consumption.

Accordingly, as per Census of India, all persons engaged in 'work' defined as participation in any economically productive activity with or without compensation, wages or profit are workers. The Reference period for determining a person as worker and non-worker is one year preceding the date of enumeration.

The Census *classifies* 'Workers' into two groups namely, *Main Workers* (those workers who had worked for the major part of the reference period, i.e., 6 months or more) and *Marginal Workers* (those workers who had not worked for the major part of the reference period i.e. less than 6 months). The *Main* workers are classified on the basis of Industrial category of workers into the following four categories: (i) Cultivators; (ii) Agricultural Labourers; (iii) Household Industry Workers; and (iv) Other Workers.

[See entry *'Non-Worker'* also.]

WORKER POPULATION RATIO

The employment-to-population ratio is defined as the proportion of an economy's working-age population that is employed. As an indicator, the employment-to-population ratio provides information on the ability of an economy to create jobs. Worker population ratio (WPR) is defined as the number of persons employed per thousand persons [WPR= No. of employed persons X 1000/ Total population]. Worker Population Ratio is an indicator used for analyzing the employment situation in the country. This is also useful in knowing the proportion of population that is actively contributing to the production of goods and services in the economy.

[*Reference:* NSSO (2005), *Report No. 515, Employment Unemployment Situation in India (Part 1), 61st Round (2004–2005)*]

WORKFARE

Government programmes which make the receipt of unemployment-related benefits (as unemployment allowance) conditional upon participation in some local work scheme.

X-INEFFICIENCY

A graphic representation of the 'gap' a firm shows in its actual and minimum costs of supplying its products. As per the traditional theory of supply, firms always operate on minimum attainable costs. As opposed to this, x-inefficiency suggests that firms typically operate at higher costs than their minimum attainable costs. This takes place due to many *inefficiencies* (such as organising the works, lack of co-ordination, lack of motivation, bureacratic rigidities etc.). Large corporates usually face this problem as they lack effective competition which could 'keep them on their toes'.

YIELD GAP

A method of comparing the performance of bonds and shares in an economy. It is defined as the average returns on shares minus the average returns on bonds.

ZERO-COUPON BOND

A bond bearing zero coupon rate (i.e. no interest) sold at a price lower than its face value and investors getting the face value price at maturity.

ZERO-SUM GAME

A situation in the *game theory* when the gains made by winners in an economic transaction is equal to the losses suffered by the losers. This is considered a special case in game theory. Most economic transactions are in some sense *positive-sum games*. But in popular discussion of economic issues, there are often examples of mistaken zero-sum mentality, such as profit comes at the expense of wages, 'higher productivity means fewer jobs', and 'imports mean fewer jobs here.'

ZERO TILLING

A relatively new farm production process, is a one-time operation in which a small drill places the seed and the fertiliser in a small furrow, saving the farmer a lot of time and other resources. At first utilised in Haryana in 1999–2000, by now it has spread to the other wheat growing states like, Punjab, Uttar Pradesh, Uttarakhand, and Bihar particularly. The technique gives comparatively higher yield (by over 5 per cent) than the conventional wheat farming.