



Improving the Investment Climate: Challenges for India and for Karnataka

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This presentation is based on various World Bank studies on Investment Climate and Business Environment issues including: India Investment Climate Assessments (2002,2004), Doing Business Indicators 2005 and the World Development Report (2005)



Investment Climate defined

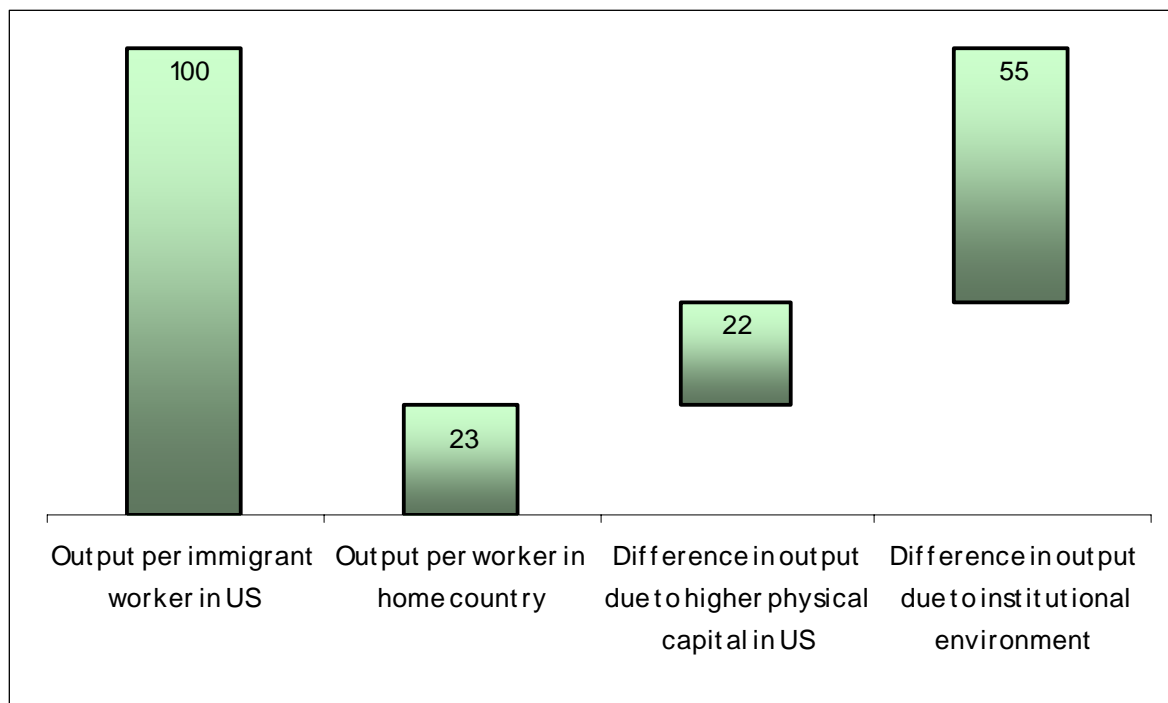
The Investment Climate comprises institutional and policy variables that have a crucial bearing on business performance, but over which individual firms have no control individually.

Key determinants of the Investment Climate include:

- ❑ the functioning of **product and factor markets** (including markets for labor, land and capital);
- ❑ sources of non-pecuniary **intra – and inter-industry externalities**;
- ❑ the **quality of public goods** (such as law and order, government regulation) and their effects on cost of borrowing, on price stability, on exchange rates via fiscal and monetary policies;
- ❑ and **physical and social infrastructure**



Why Investment Climate?



Source: Calculations based on Hendricks (2002).

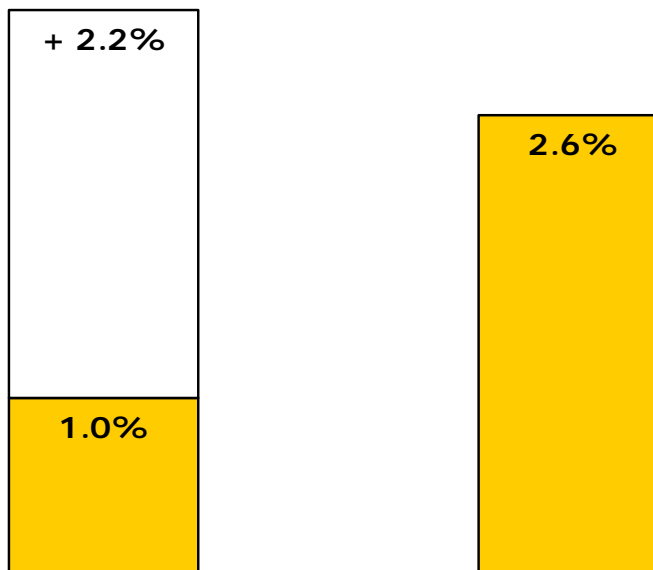
Factor accumulation accounts for only a fraction of income differences (in percent)



Reform pays off

Reforms to reach the top quartile of countries would add 2.2 percentage points annual growth

Actual Growth



Bottom quartile

Top quartile

Ease of Doing Business indicator



Doing Business Indicators: Methodology

- **Measure government regulation and protection of property rights and their effect on businesses, especially SMEs**
 - Document degree of regulations (e.g. no. of procedures etc)
 - Gauge regulatory outcomes (e.g. Time and cost to enforce contract)
 - Measure extent of legal protection (e.g. scope of assets used as collateral)
- **Based on research of laws and regulation with input and verification of government officials, lawyers, business consultants and other professionals; uses factual information and involves continual interactions with local respondents to avoid misinterpretation**
- **Three limitations**
 - In some cases uses the data from most populous city and may not be representative of the whole country
 - Focus on specific business form and specific case assumptions
 - Some indicators, such as time, involve an element of judgments of the expert respondent; median values of responses taken



Investment Climate Survey: Methodology

- **Firm-level survey: 1856 manufacturing establishments sampled from 40 cities, from each of 12 of India's 15 largest states.**
- **Between them the 12 states account for well over 90 percent of India's industrial GDP; the 3 or 4 cities covered in each state also accounted for the bulk of manufacturing outputs of their respective states**
- **Sampling frame collected from business association lists, directory of SSIs, ASI, DIPP – GoI etc.**
- **In each city, samples were drawn mainly from exporting or import competing manufacturing industries: food, textiles, garments, leather goods, drugs and pharmaceuticals, chemical, consumer electronics, electrical white goods, auto parts, fabricated metals, and machinery**
- **At the state level – the top 4-5 sectors of the state's economy are chosen to provide statistical significance**
- **Random sampling with two reserve samples**

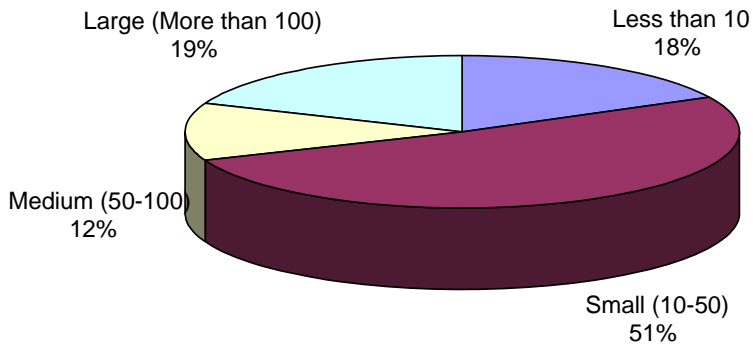


I. How does Karnataka compare with other states on investment climate indicators?

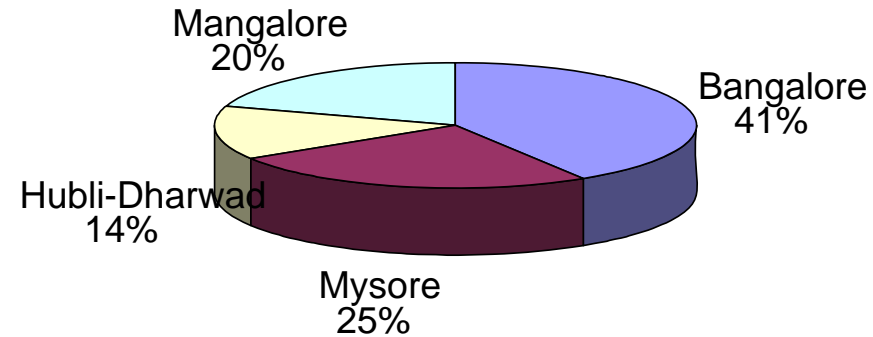


Sampling profile of Karnataka

Size profile of surveyed firms



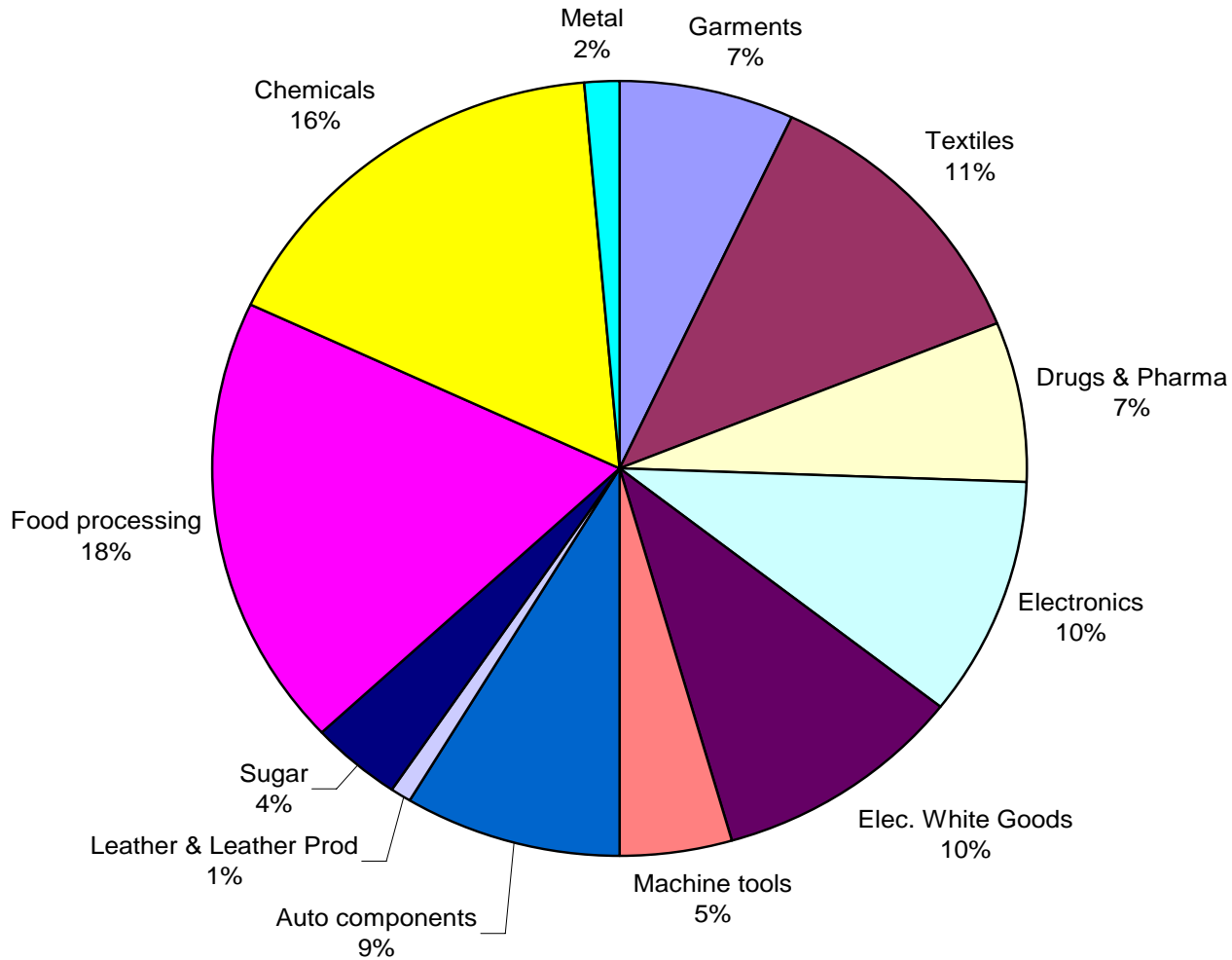
City-wise distribution of surveyed firms



Note: 200 firms surveyed



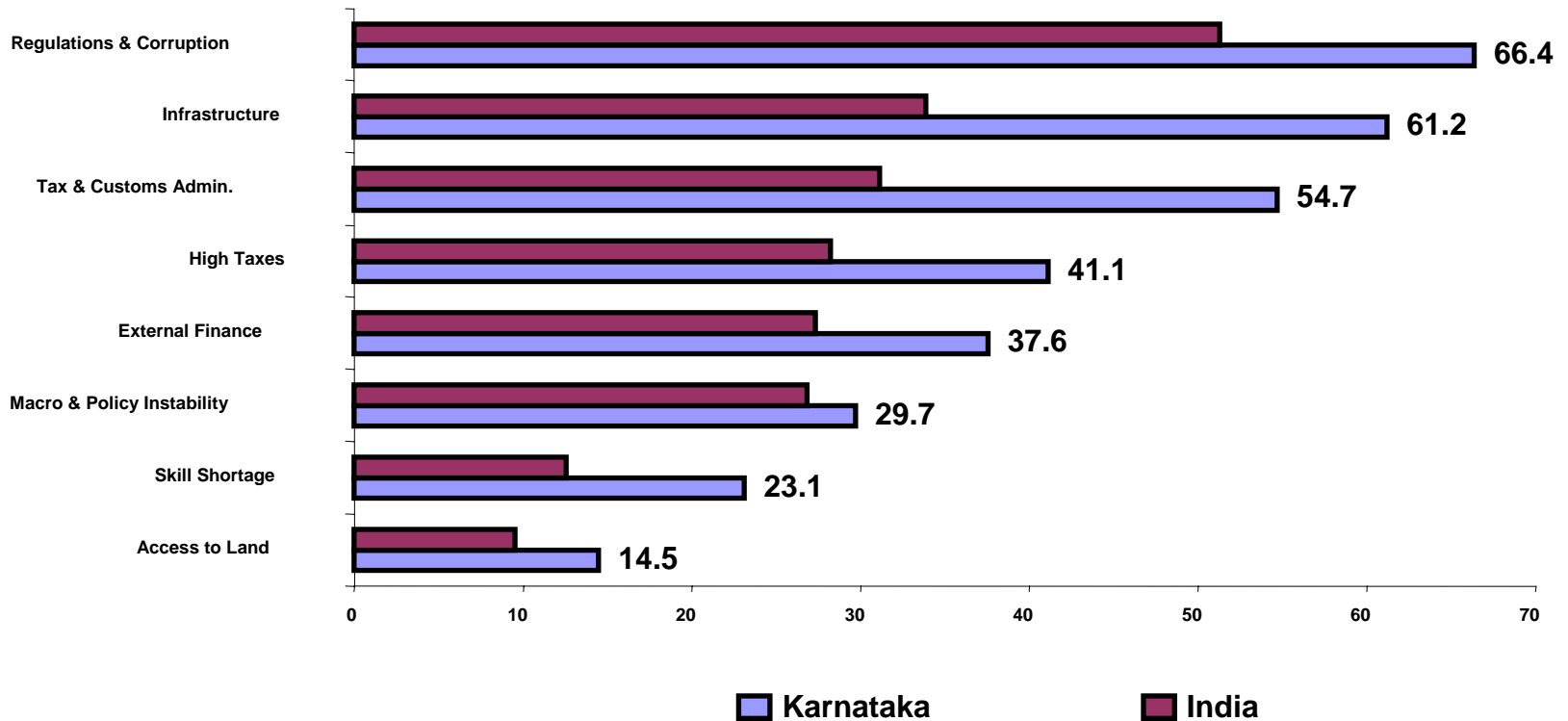
Sampling profile of Karnataka (contd.)





Major perceived constraints

Percent of respondents identifying factor as major or severe obstacle - Karnataka





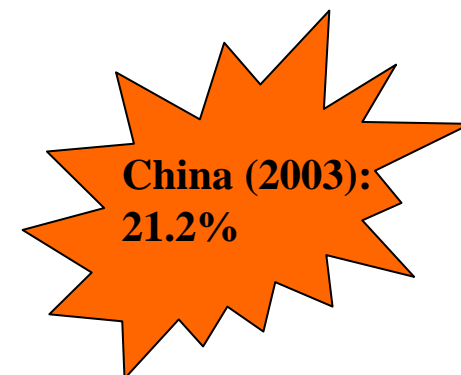
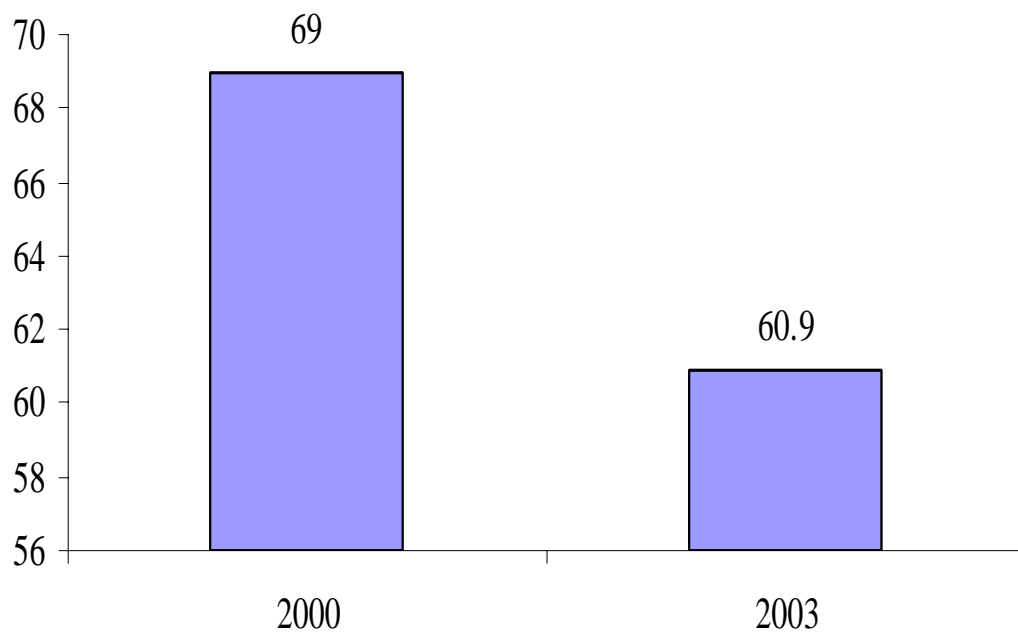
Key IC indicators for Karnataka:

A. Infrastructure



Access to power

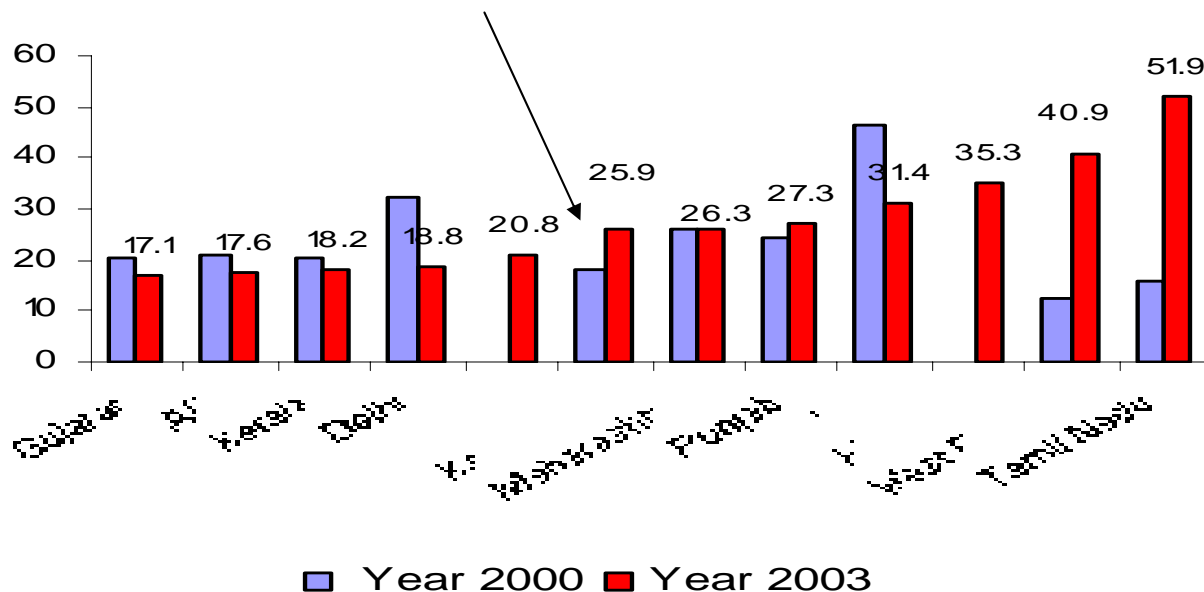
Percent of Indian firms running own generators





Infrastructure: Access to electricity at reasonable cost

Percent of Power Supply from Own Generators



**Brazil
(2003):
1.6%**

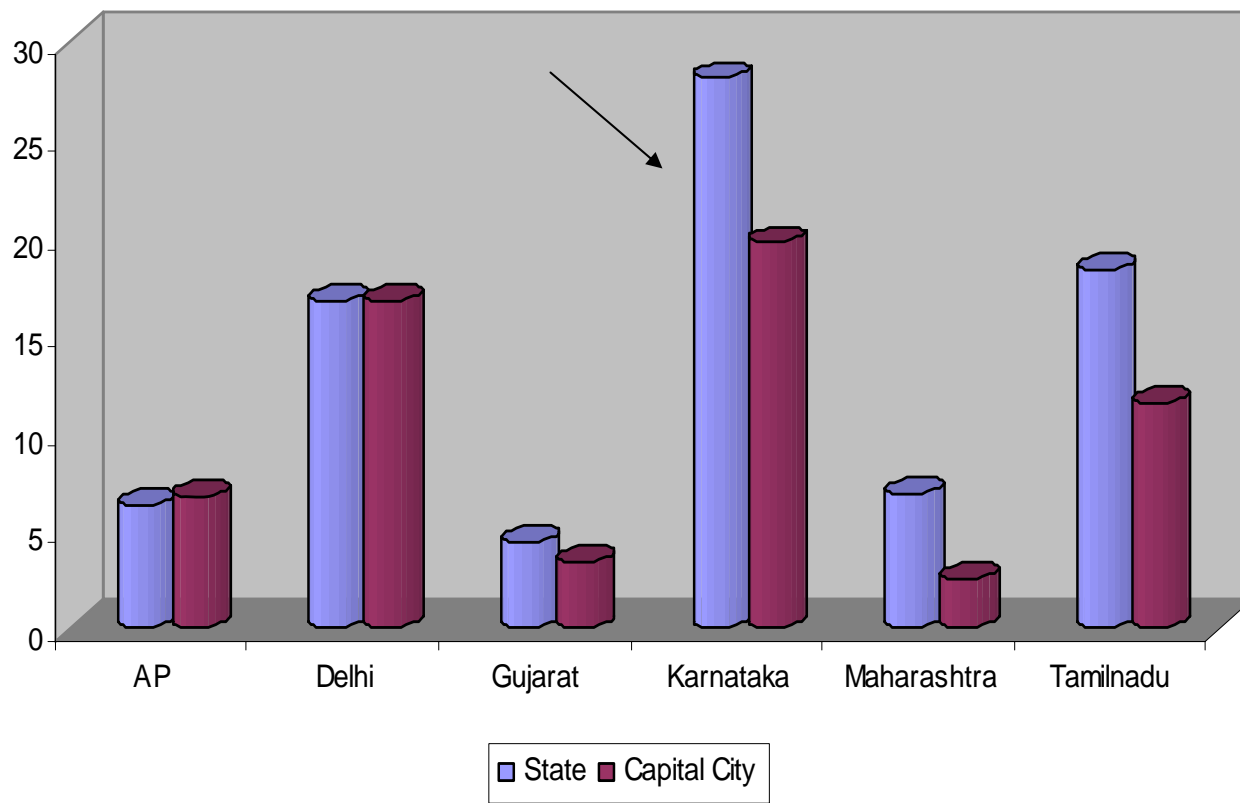
**China (2003):
1.5%**

Source: India Investment Climate Assessment, 2004



Reliability of power

Average Number of Power Outages During the Month Preceding the Survey

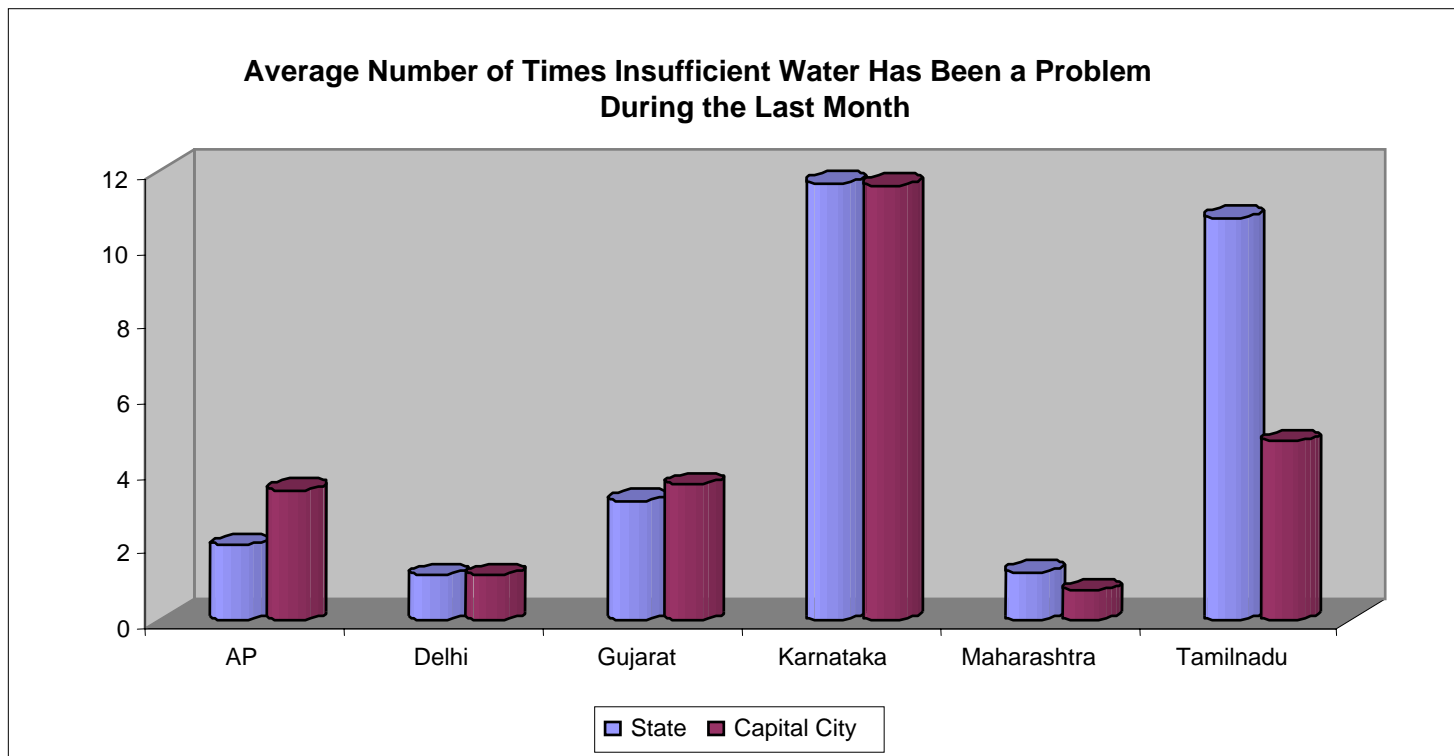


**Brazil (2003):
4.1**

**China (2003):
2.1**



Water



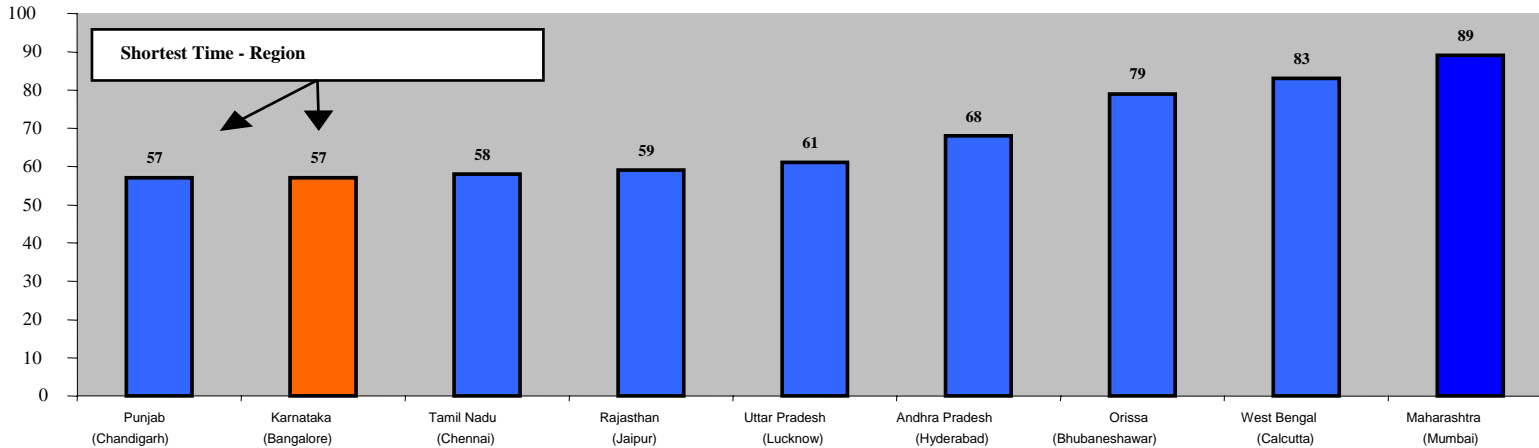


B. Business Regulation

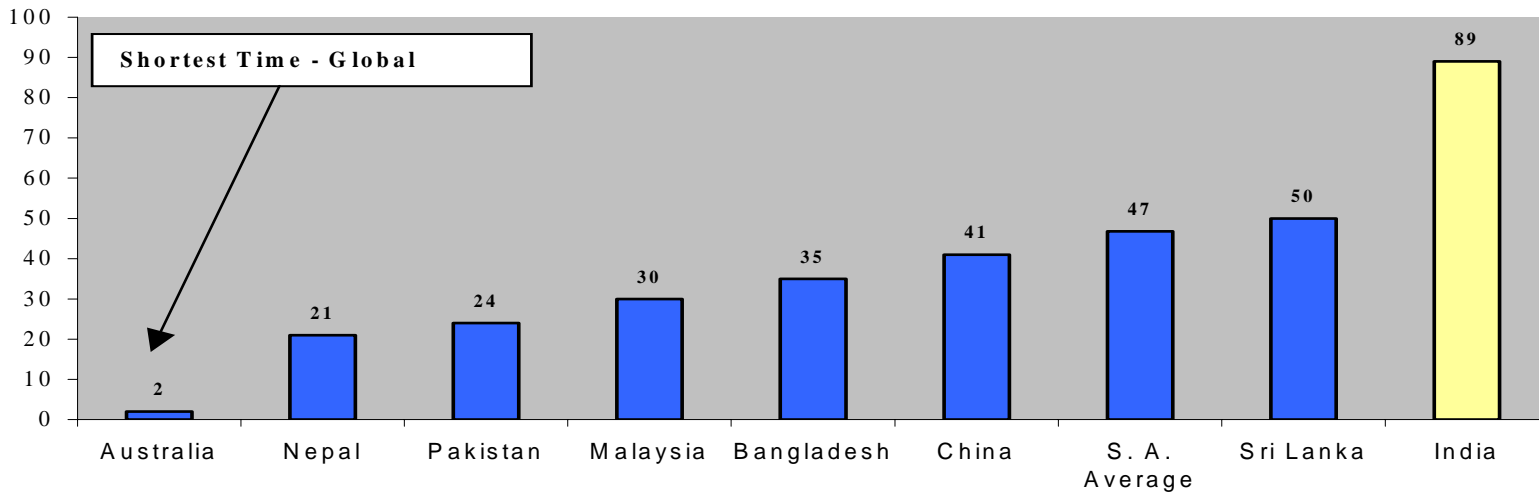


Entry regulation

Time to Start a Business (Days)



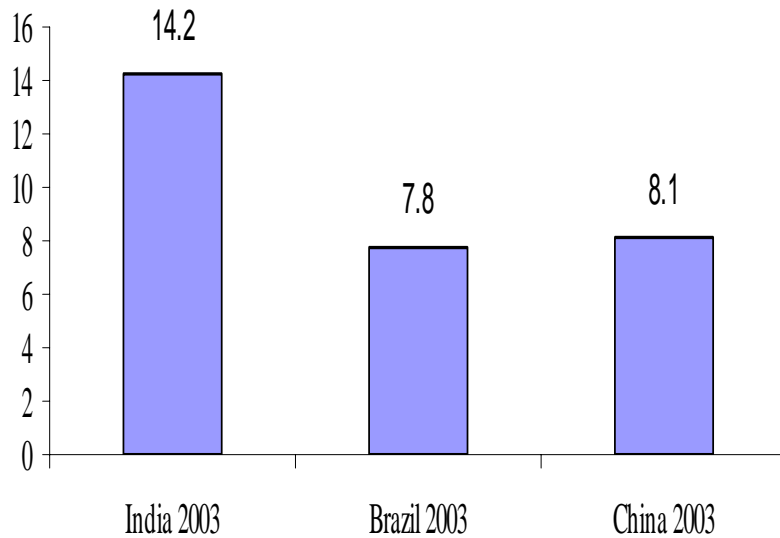
Time to Start a Business (Days)



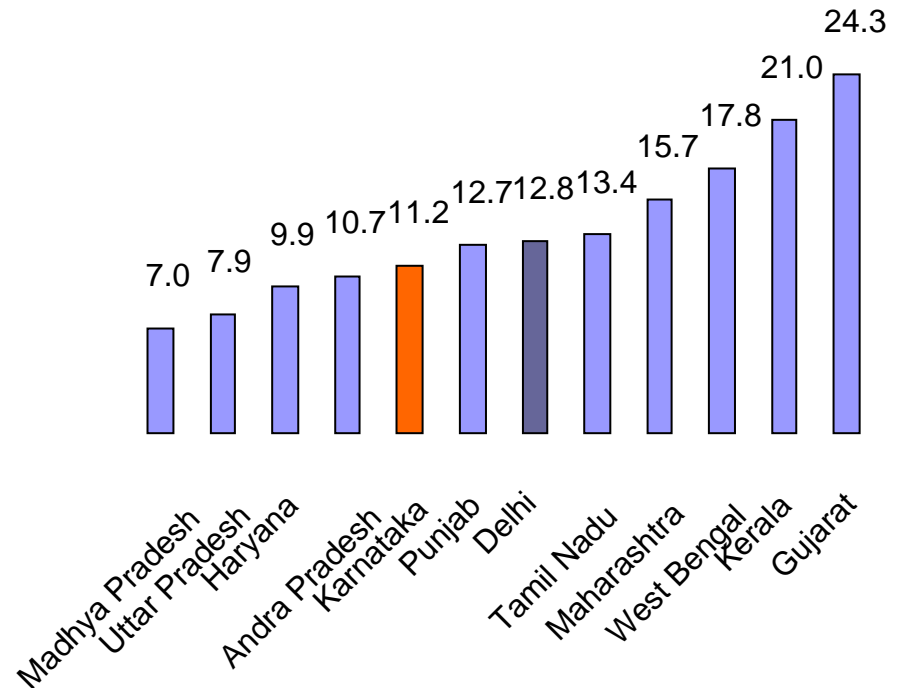


Burden of regulation

Senior management time spent dealing with regulations (%)



Senior management time spent dealing with regulations (%)

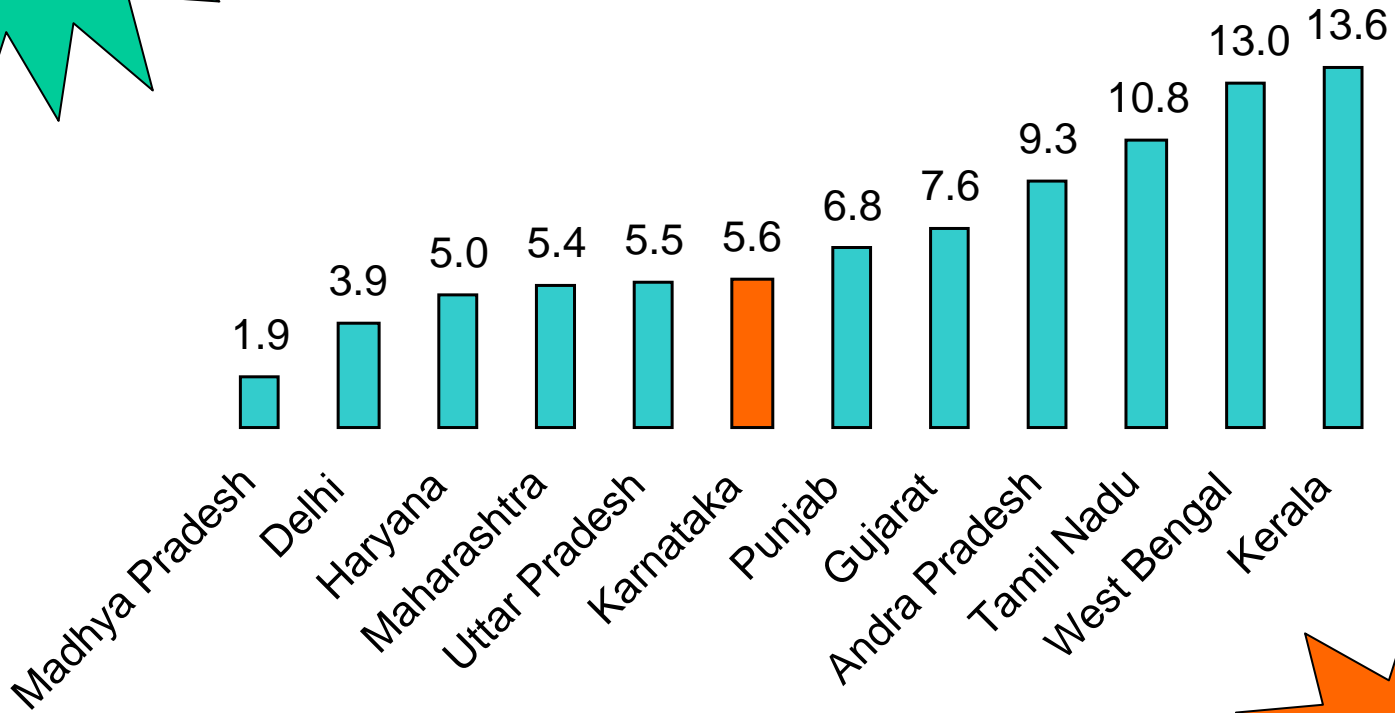




Inspector Raj

Number of inspections by government officials

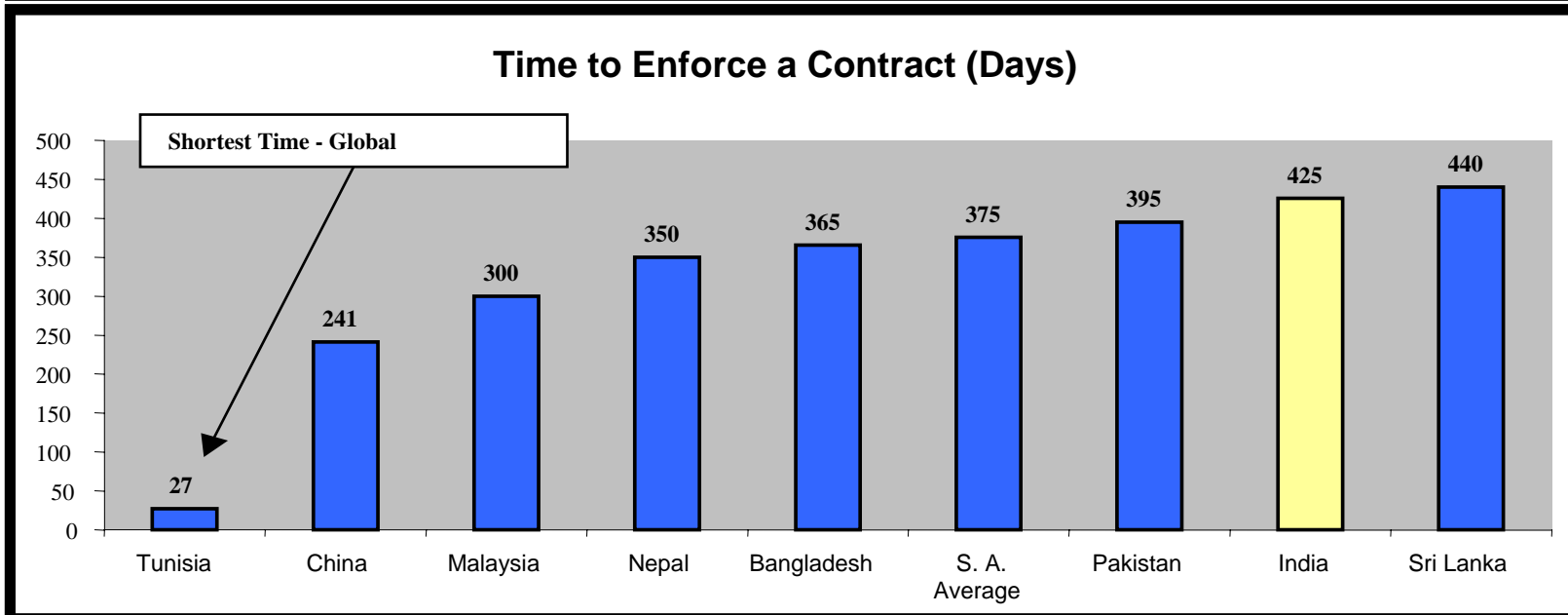
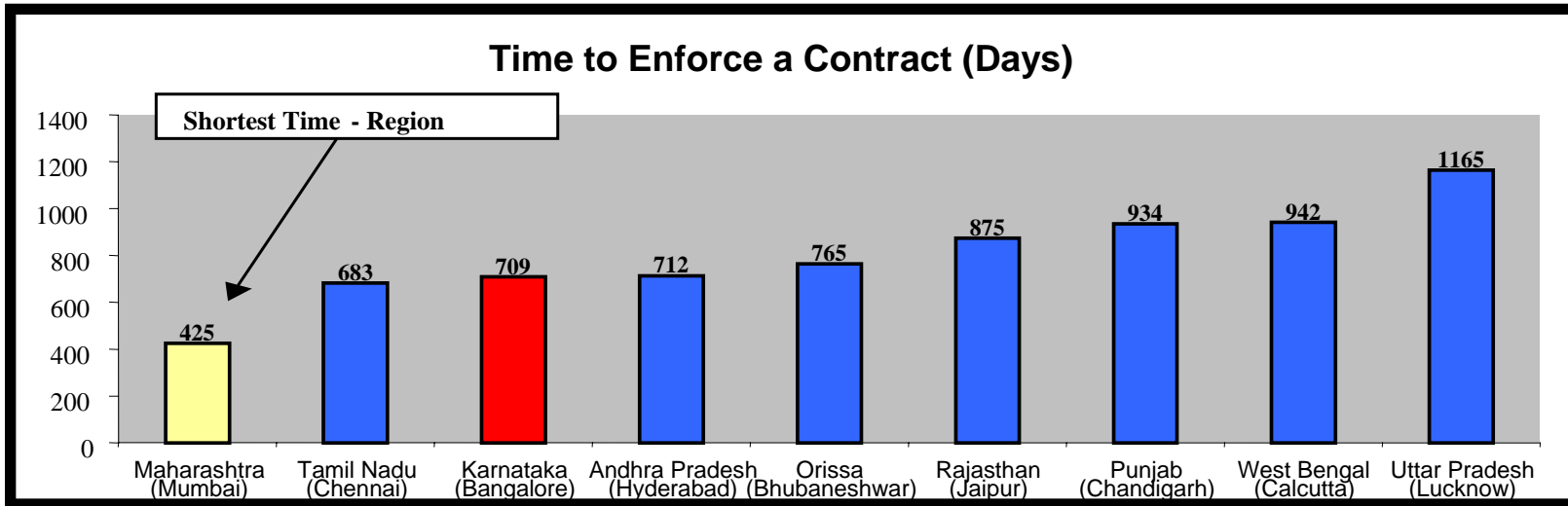
**Brazil
(2003): 7.8**



**China (2003):
26.7**



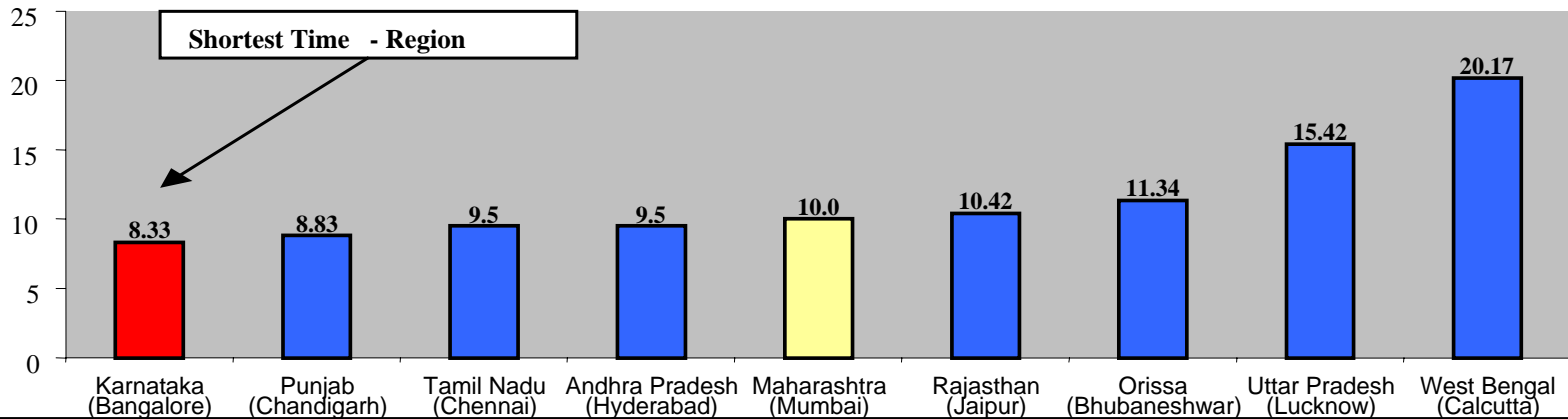
Enforcing contracts: Time to enforce a contract



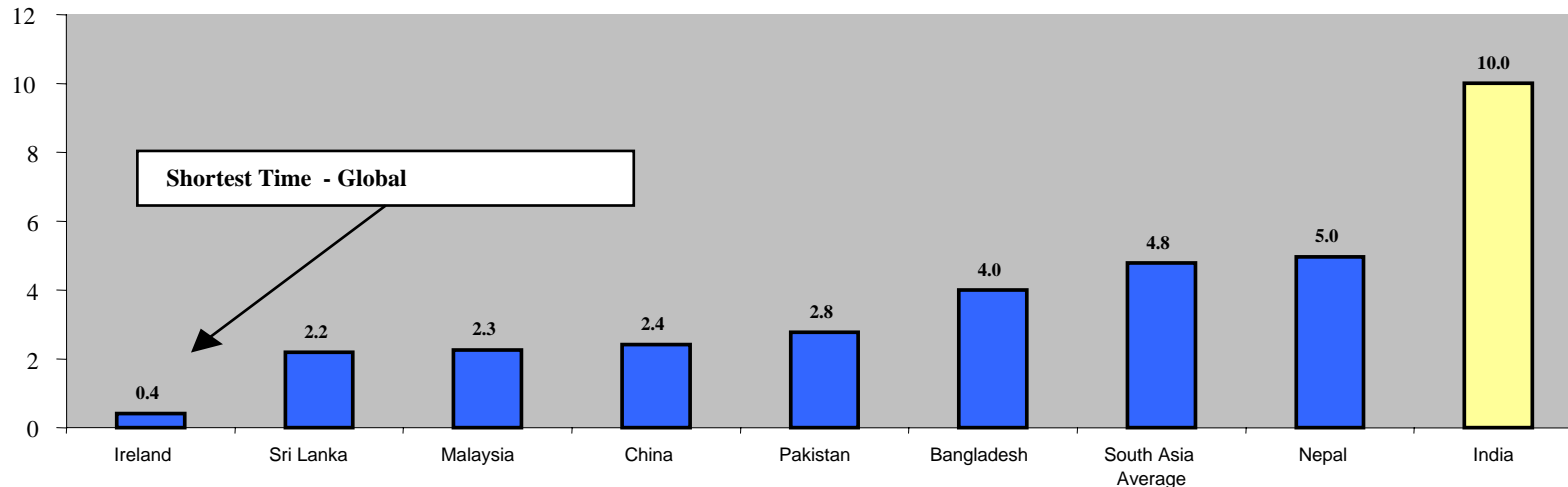


Bankruptcy: Time to go through insolvency

Time to go through Insolvency (Years) – Data for India



Time to go through Insolvency (Years) – Global data



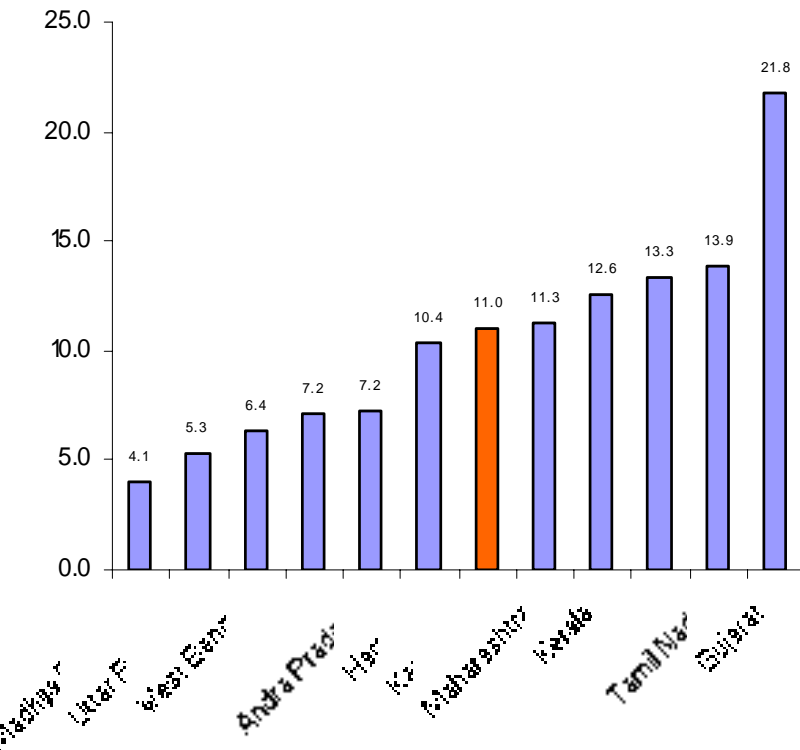


C. Labour

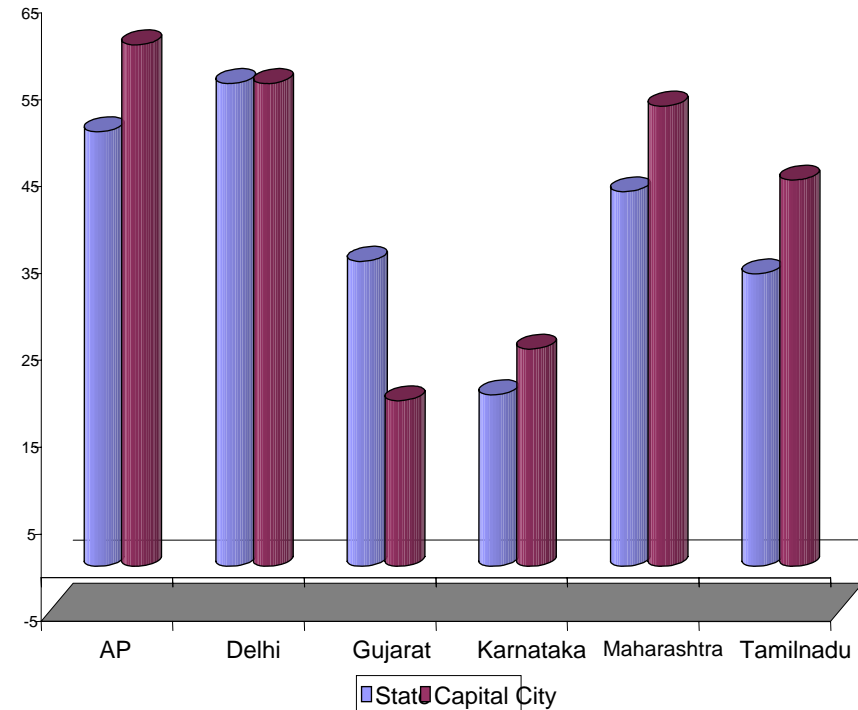


Labor regulation as a bottleneck to business performance

Reported overstaffing rates (%)



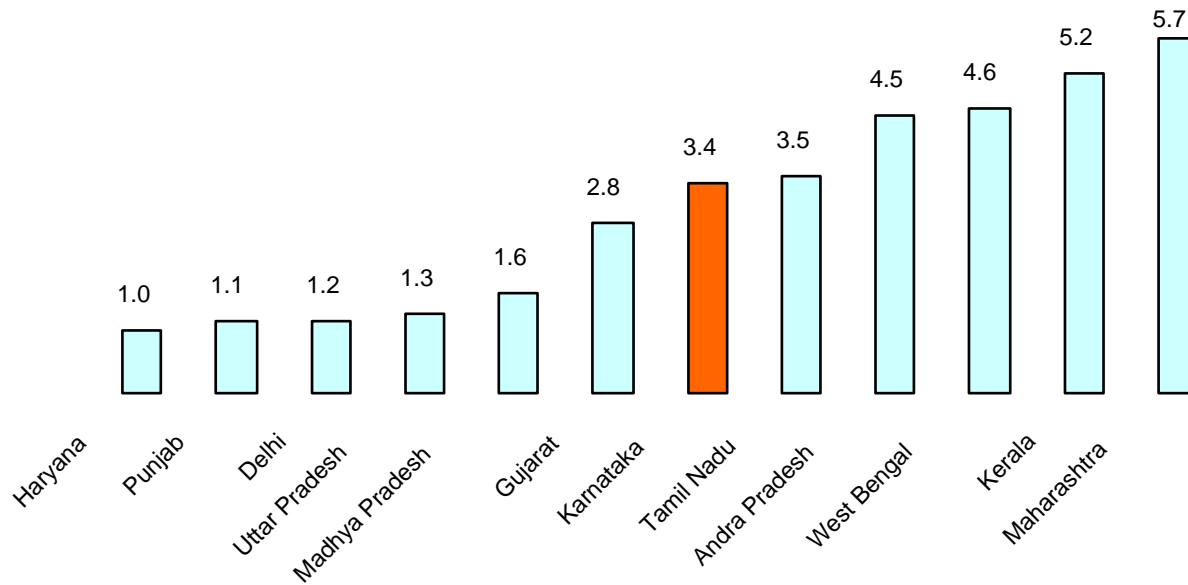
Percentage of Firms Perceiving Lay-off Regulations, Workers' Union and Govt./Political Pressure as Constraints





Skills availability

Days needed to fill a skilled vacancy



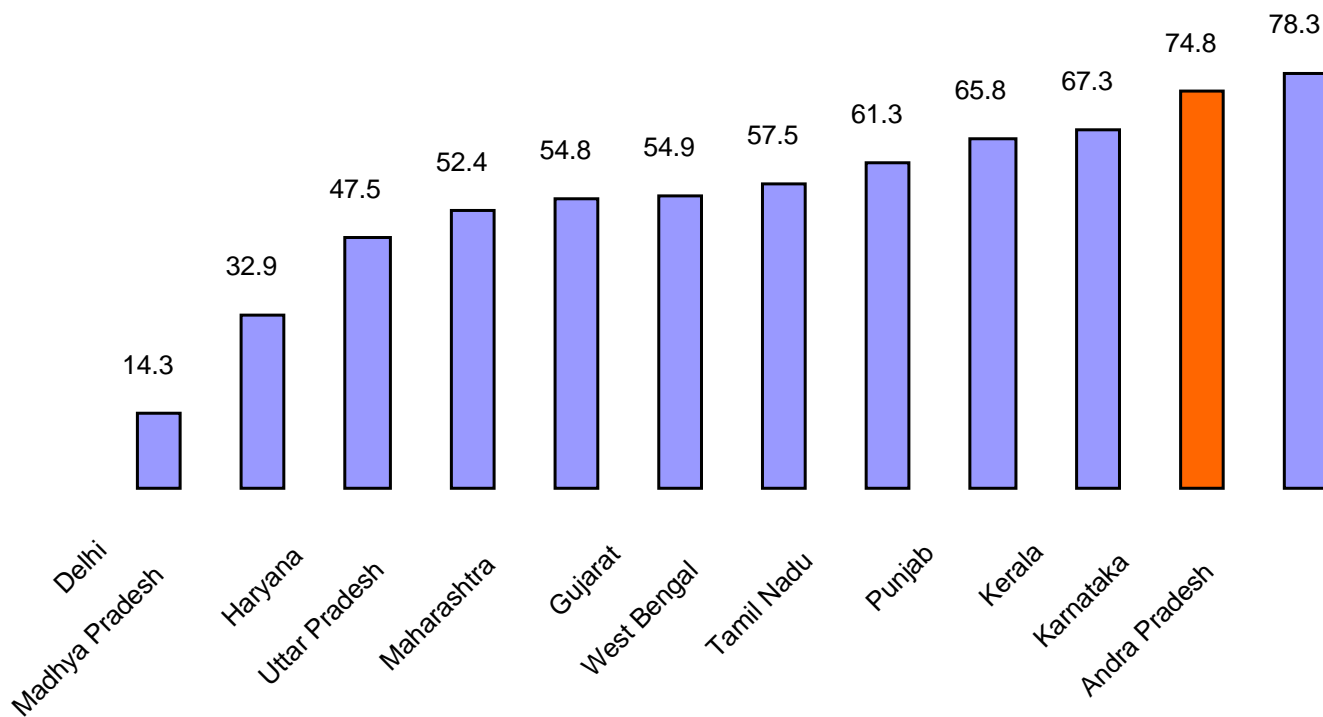


D. Access to finance



Overdraft facilities

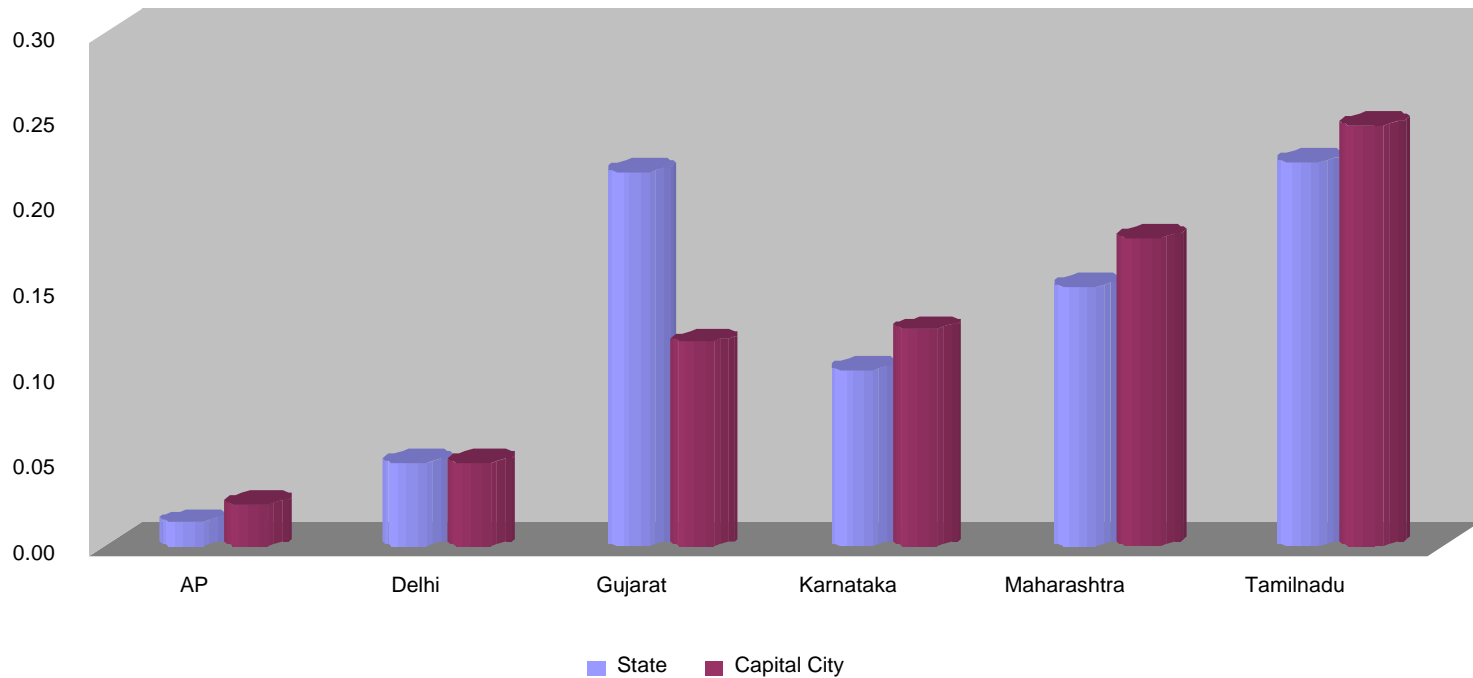
Establishments with bank
overdraft facility(%)





E. Law and order

Share of Firms Unsatisfied with the Law & Order of the Locality





Need to catch up

- The states with poorer investment climate need to catch-up with the better states
- But the better states also need to catch up with their counterparts abroad – on some key regulatory indicators, as well as in providing more reliable and infrastructure (particularly power) at more competitive prices
- If each Indian state could attain the best practice in India in terms of investment climate, the economy would grow about 2 percentage points faster.