

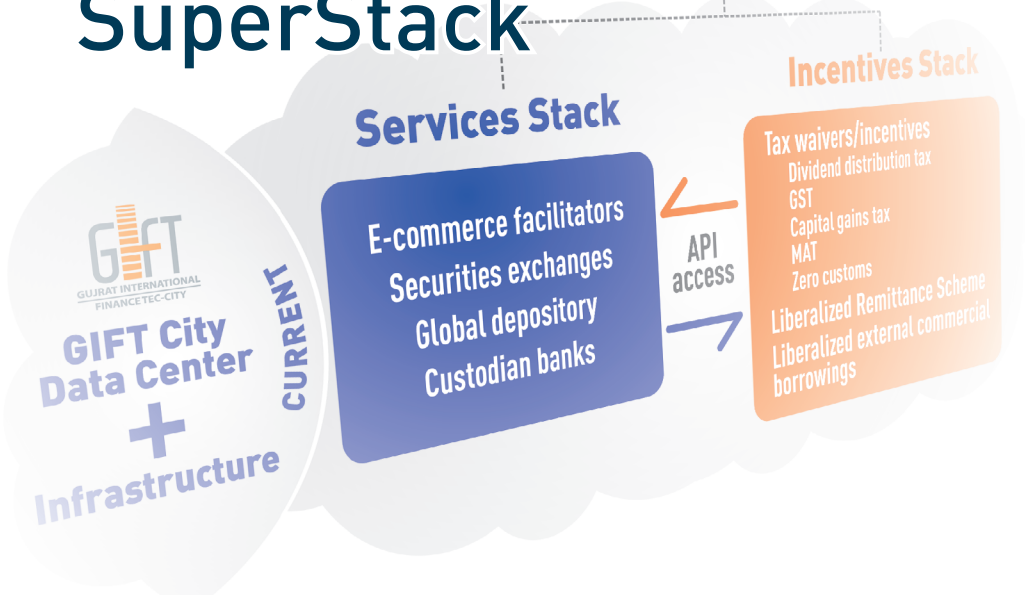
Reimagining GIFT City

as

Digital SuperStack



Digital SuperStack



A brief by



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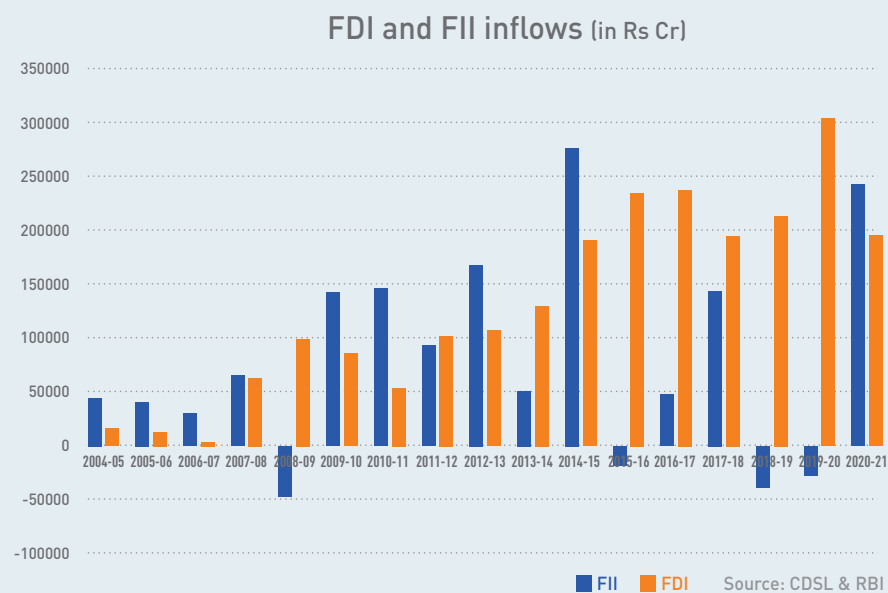
Reimagining GIFT City as Digital SuperStack

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|--|----|
| 1. Reimagining GIFT City as Digital SuperStack | 01 |
| 2. GIFT City: concept vs reality | 03 |
| 3. Paradigm shift: from location-incentives model to a transaction-incentives SuperStack | 07 |
| 4. Making the GIFT City digital SuperStack work | 09 |

Reimagining GIFT City as Digital SuperStack

In 2007, the Indian government set up the International Financial Service Centre (IFSC) at Gujarat International Fin-Tec City (GIFT City) to develop as a center for global finance. In the last six-odd years the city has seen slow progress. It is time to reinvent GIFT City—not only as a physical location for global finance, but as a digital destination for global financial transactions.

Global finance has changed in the last 14 years—from physical to digital. Establishing a new IFSC today cannot be about old world attributes such as physical locations, permanent establishments of companies in a physical location, or even the movement of expertise or knowledge; all these are old world. **The focus of a new world IFSC will have to be reimagined away from its current locational proposition to being a Transactions Platform that captures global financial transactions of investment and, more importantly, digital trade.**



This shift of both flows is possible in the current digital world. All it requires is a **reimagination of incentives**. The reimagination has to envisage the future flow of global transactions from the outsider's perspective, different from the past perspective of investment inflows. GIFT City has to let go of the obsession with merely attracting and capturing inflows into India. Anchoring and competing against the past has not resulted in success in the last 14 years. For any chance of future success, an international financial center has to think of itself as an enabler of global transactions and position itself to the international investor on a futuristic proposition.

\$ million

Table III.1. Export of digitally deliverable services, by region and by level of development, 2005 and 2018

Region	2005	2018	Compound annual growth rate 2005-2018 (per cent)
World	1179430	2931400	7
Developed economies	989320	2232100	6
Developing economies	178030	659870	11
Africa	10860	26790	7
Asia and Oceania	145150	575920	11
East Asia	97130	341570	10
South Asia	39260	140310	10
South-East Asia	37310	161330	12
West Asia	25340	73860	9
Latin America and the Caribbean	22030	57160	8
Transition economies	12080	39430	10
LDCs	2100	7460	10

Source: UNCTADStat.

GIFT City: concept vs reality

GIFT City was envisaged as an integrated development centre. Built on 886 acres—a conducive multi-service SEZ spread over 261 acres and an exclusive Domestic Tariff Area (DTA) spread over an additional 625 acres—in the outskirts of Gandhinagar in Gujarat it was conceptualised by the then Chief Minister of Gujarat, Narendra Modi. It was provided recognition and impetus by the central government in 2015 soon after he became Prime Minister.

The plan envisaged building 62 million square feet built-up area consisting of commercial space spread over 67 percent, residential space of 22 percent, and social space of 11 percent. The whole focus was to develop real estate and create IFSC. But an IFSC as a global city has both soft and hard infrastructure. Soft infrastructure includes people, expertise, climate, environment, and quality of life, among other things; hard infrastructure includes buildings, offices, schools and airports.

It takes decades to build an ecosystem that enables soft infrastructure. The hard infrastructure is a function of the development of the soft; it follows or keeps pace with it and hence leads to a Catch-22 situation—what to develop first? Cities and governments have tried out several options in the absence of a one-size-fits-all model.

What worked in the past cannot be replicated in the present without considering current trends and future needs. China tried to create its own Silicon Valley but did not succeed until Kai-Fu Lee built an ecosystem of AI engineers and expertise in Beijing's Zhongguancun neighbourhood.

Beijing's Silicon Valley did not succeed until it reached a critical mass of experts; their research was not funded by the Chinese government and VCs.

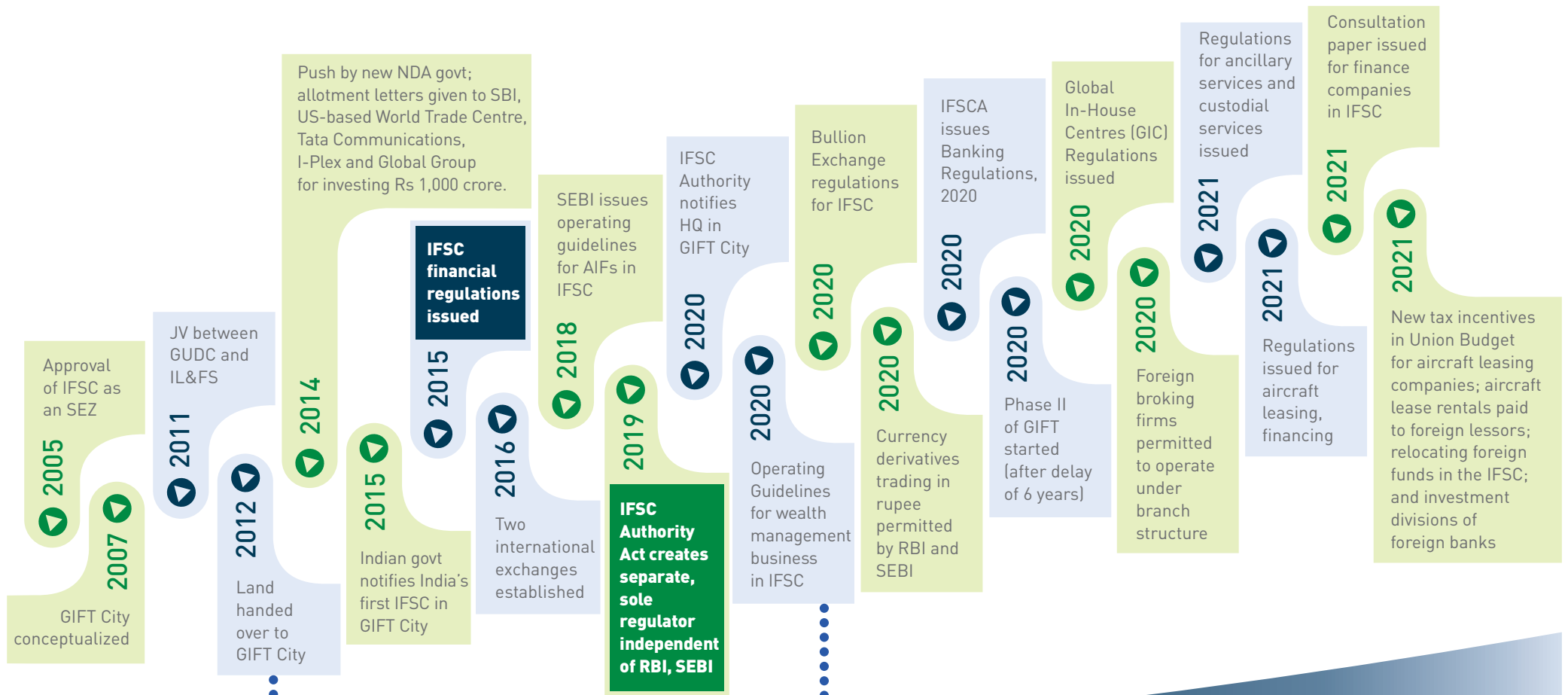
Investment inflows are proving to be a mirage; GIFT City should focus on global transactions and investment.

International finance no longer depends on physical amenities as people with expertise may already be working from remote locations. Most transactions these days are digital. The crucial issues should be taxation and the incentives being given to initiate and fulfill each transaction. Expertise is location-independent; it can be plugged in as an intervention or as an algorithm.

This shift in finance has been long recognized by entrepreneurs and startups; yet, it is not being appreciated by regulators and policy makers. They continue to chase and build physical models of a financial services world that is already overwhelmingly digital.

Financial services have a huge potential for growth—a dedicated hub can contribute significantly to advancing this sector. In 2015, the financial sector provided 5 million jobs and 5 percent of the GDP. Between 2007 and 2020, the contribution to GDP of capital markets and trading services rose from 1 percent to 10 percent, and of market capitalisation from USD 7 billion to USD 75 billion. With the right plan and the right incentives, it is possible to increase the GDP contribution of financial services to 15 percent of GDP and employment to 11 million.

Much effort over the years...



Nothing moved for 5 years

Operating structures and regulations were put in place in the next 8 years

Properly re-imagined, GIFT City is poised for success

Paradigm shift: from location-incentives model to a transaction-incentives SuperStack

In a recent report published by the Global Financial Centres Index from London, GIFT City is ranked third among 15 centres that are likely to grow in significance over the next few years. But its growth as a physical location is limited by physical and cultural constraints. In today's digital world physical location matters little. Hedge fund managers may register an office in an offshore tax haven and operate from a beach in Honduras or a hacienda lined with orange trees in Spain. **Intellectual power is defined by algorithms; physical proximity is not needed for today's international finance transactions.**

An IFSC caters to customers outside the jurisdiction of the domestic economy. It deals with the flow of finance and financial products and services across borders. IFSC, as envisaged in the Indian context, "is a jurisdiction that provides financial services to non-residents and residents (institutions), in any currency other than Indian Rupee (INR)". IFSC's mandate is to undertake financial services transactions that are currently handled outside India by overseas financial institutions and overseas branches/subsidiaries of Indian financial institutions. Unfortunately, even the latest report on revamping GIFT City focuses on global flows into India, instead of looking at the global opportunity of capturing global transactions. The focus continued to be incoming investment from NRIs.

Initially, India in its pursuit of emerging as a major economic power had built GIFT City as a way to attract overseas Indians back to India transforming India into a financial hub. **This objective needs to change—from attracting people, companies and offices to attracting transactions and flow of capital movement.** It is difficult to make people shift from places that they have been comfortable with for years; they would want a better climate, environment, and facilities. **Instead of trying to physically replicate a Singapore, Dubai or London in GIFT City, India should create a world class digital infrastructure, and create a digital SuperStack** that houses both the services stack and incentives stack of the tax and other incentives needed to attract global transactions through GIFT City. All that is needed is a data center and public-spirited technologies to come together and create the digital SuperStack, very similar to the UPI digital stack for payment transactions between banks and digital wallets. As with the UPI stack, the services and incentives stacks will talk to each other and the myriad users of the system through APIs.

Making the GIFT City digital SuperStack work

The base of this digital SuperStack has to be an Indian custodian bank that can provide global wealth management services in an investor's currency of choice. This would be possible in the GIFT City SuperStack if India's banking regulator, RBI, allows licensing of Indian custodian bank licenses under a new differentiated banking licensing scheme.

Businesses such as re-insurance, insurance, banking services, investment in equities and commodities will be transacted through this digital SuperStack. Stock exchanges and other critical service providers will plug into this SuperStack to make the process seamless.

To get a critical mass of transactions and volume into the GIFT City SuperStack, the focus of the regulations need to shift; otherwise, GIFT City will remain a non-starter. Many intermediaries including banks and custodians are sitting on the sidelines waiting for some visibility of business to justify investments into a financial centre where business remains most uncertain, and where the lead time to volume and clients remains uncertain and undefined.

It would be far more sensible and make greater business sense to permit intermediaries (banks, custodians, brokers and fund managers) in India to set up branches in GIFT City, after regulatory clearances as applicable, than to establish a new company with extensive capitalisation in GIFT City. These branches will specifically cater only to foreign investors or overseas investors and work through the digital SuperStack.

A critical mass already exists of intermediaries providing some of the services needed in an IFSC. Instead of asking them to create new entities and distribute that expertise over multiple entities, incentives should be provided to transact at the branch level. With the base capitalisation already in place among these intermediaries from India, only incremental capitalisation should be stipulated, linked to business volume similar to the prudential norms that are applied to banks.

Reimagining GIFT City as Digital SuperStack

Current Incentives model

Tax waivers or incentives

- ▶▶ Dividend distribution tax
- ▶▶ GST
- ▶▶ Capital gains
- ▶▶ MAT

Liberalized Remittance Scheme

Liberalized external commercial borrowings

Zero customs duty

Yet interest has been muted



- ▶▶ **Need to set up new company**
- ▶▶ **Set up new office**
- ▶▶ **Transfer skilled personnel**

Global Trends

- 1 IFSCs have evolved from physical locations to digital abstractions
- 2 International finance craves incentives for transactions, not for corporations
- 3 Digital transactions shift to wherever the incentives are



Futuristic Transactional Stack model

Through a UPI-like stack of APIs, allow global finance firms to securely

- ▶▶ Identify
- ▶▶ Validate
- ▶▶ Authenticate

Remote ANYTIME, ANYWHERE global access to GIFT City's existing secure and cutting edge world-class data center and allied infrastructure

A viable, differentiated proposition



- ▶▶ **Securities exchanges**
- ▶▶ **Banks, NBFCs and other finance companies**
- ▶▶ **Custodians**
- ▶▶ **Insurance companies**

