



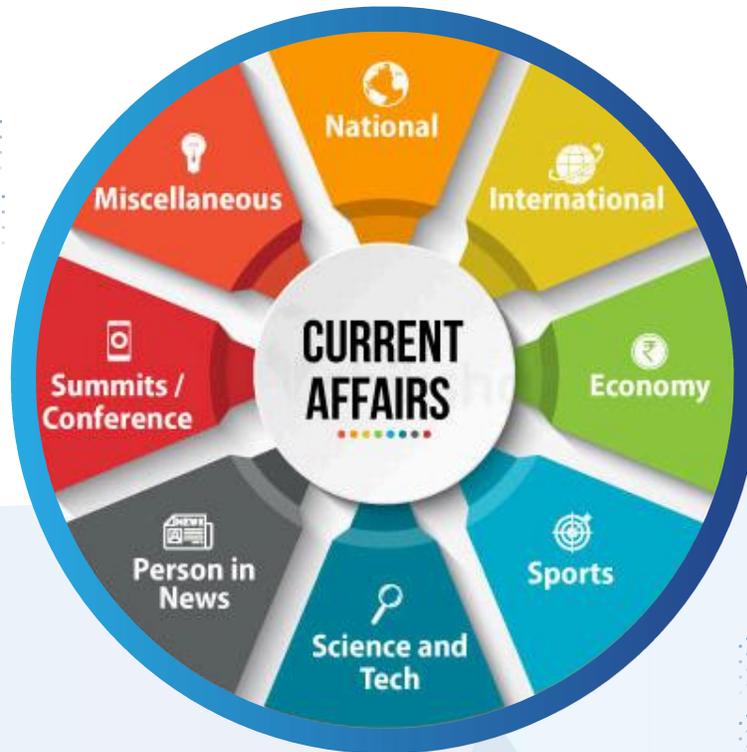
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VIDHVATH IAS KAS ACADEMY
&
STUDY CENTRE

DAILY CURRENT AFFAIRS

FOR UPSC CIVIL SERVICE EXAMINATION

DATE: 1/07/2025 (TUESDAY)



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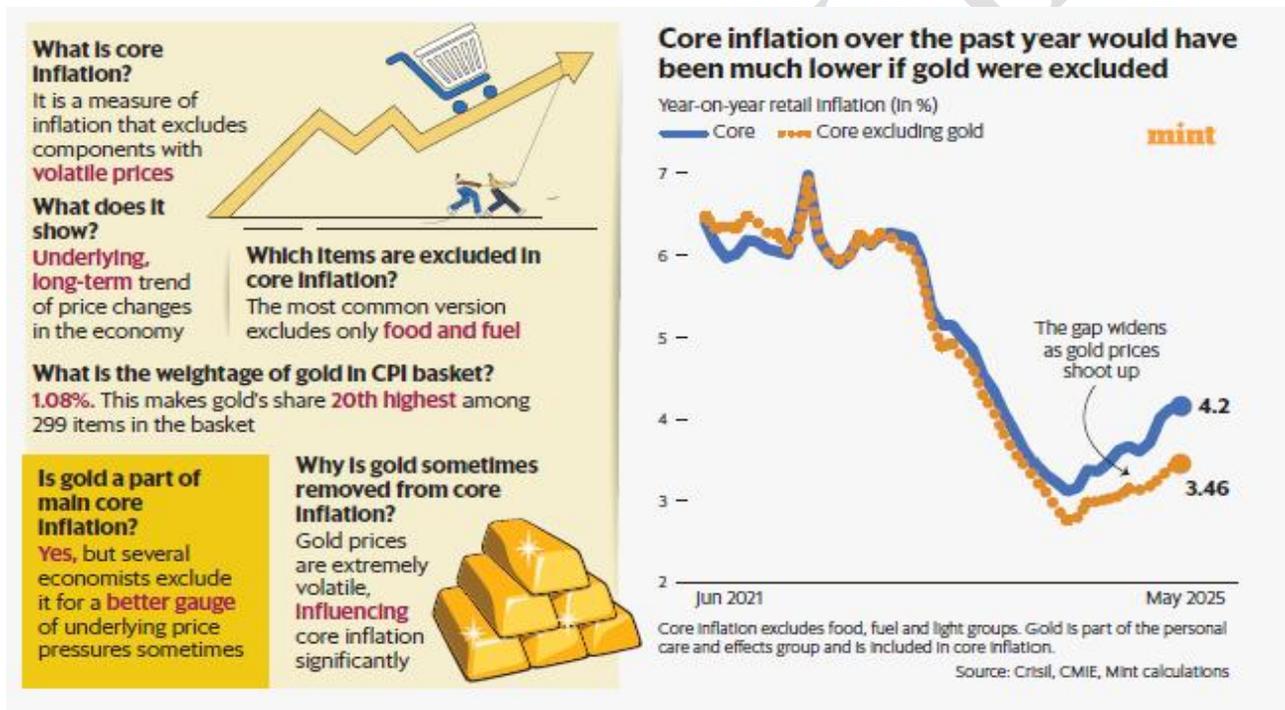
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I. Why Gold Price Swings Distort Inflation Trends

1. Gold's Role in India's CPI and Inflation Measurement

- Gold has a **1.08% weight** in the **Consumer Price Index (CPI)** basket—20th highest among 299 items.
- Despite its relatively modest weight, gold's **high price volatility** makes it a **distorting factor** in inflation measurement, especially in **core inflation**.
- **Core inflation** aims to reflect **long-term underlying price trends**, excluding **volatile items** like **food and fuel**.
- However, gold is sometimes included in the core inflation metric, although many economists argue for its exclusion to avoid distorted signals.



2. Volatility of Gold Prices vs. Other CPI Items

- Between **FY2016–FY2025**, gold showed a **standard deviation of 12.42%**, making it **one of the most volatile items** in the CPI basket.
- This is much higher than other essentials like **mustard oil (5.69%)**, **petrol (2.19%)**, or **wheat/flour (2.56%)**.
- The volatility comes from **global influences** rather than domestic supply-demand factors, limiting RBI's control over its inflationary impact.



3. Impact on Core Inflation and Policy Misjudgment

- As per a Crisil report, **core inflation in May 2025** was **4.2%**; however, **excluding gold**, it would have been **3.4%**.
- This **0.8 percentage point gap** due to gold inflation **misguides monetary policy** if RBI or policymakers do not adjust for it.
- Since gold prices react more to **global uncertainties** (geopolitics, currency fluctuations), their inflationary signals are **not reflective of domestic economic health**.

4. India's Gold Demand: Tradition Meets Investment

- India had **second-highest total gold demand** in 2024 (**803 tonnes**), after China (816 tonnes), according to the **World Gold Council**.
- **Gold jewellery demand** in India was **563 tonnes** (highest globally), while **investment demand** in bars and coins rose **29% YoY** to **239 tonnes** in 2024.
- The rise in demand followed the **cut in gold import duty from 15% to 6%** in Union Budget 2024.

5. Legal and Policy Implications

- The **Monetary Policy Framework Agreement (2016)** mandates the **RBI to maintain CPI inflation at 4% (+/-2%)**.
- Distorted CPI due to gold volatility may lead to **misguided repo rate decisions**, impacting borrowing costs, investments, and growth.
- Calls for a **recalibrated definition of core inflation** (excluding gold and silver) are gaining strength to improve monetary targeting.

Key Definitions (For UPSC Notes)

- **CPI (Consumer Price Index):** Measures average change in prices paid by consumers for goods and services over time.
- **Core Inflation:** Inflation metric that **excludes volatile items** like food and fuel to show underlying trends.
- **Standard Deviation:** A statistical measure indicating the amount of variation or dispersion in a dataset.

Conclusion

Gold's deep socio-cultural and investment relevance in India gives it a prominent spot in the CPI basket. However, its **extreme volatility**, driven largely by **global economic factors**, often leads to **misleading inflation readings**, particularly in **core inflation**. Policymakers must consider **excluding gold from the core inflation basket** or interpreting its contribution with caution to **ensure accurate macroeconomic assessments** and **appropriate monetary policy responses**.



2. Cloud of External Factors May Rain on Growth: RBI

1. External Headwinds Threaten India's Growth Outlook

- **RBI Governor Sanjay Malhotra**, in the **Financial Stability Report (FSR)**, warned that **external factors** such as **global trade fragmentation, geopolitical tensions, climate change, and technological disruptions** pose significant **downside risks** to India's growth.
- Despite strong **domestic macroeconomic fundamentals**, India's **external vulnerability** remains a concern in an increasingly volatile global economic environment.

2. Tariff and Trade Shocks: A Major Concern

- **Trade protectionism**, especially from the US, has emerged as a challenge.
 - Ex-US President Donald Trump imposed a **27% tariff on Indian exports** (paused for 90 days) and retained a **10% baseline tariff**, hurting Indian supply chains.
- These tariff barriers disrupt **global value chains (GVCs)**, reduce export competitiveness, and **impact manufacturing and employment** in India.

3. Geopolitical Conflicts and Energy Price Volatility

- The **Israel-Iran conflict** recently led to a **surge in crude oil prices**, a key input for India, which **imports nearly 90% of its energy needs**.
- A sustained rise in oil prices increases the **current account deficit (CAD)** and can **fuel inflation** if the burden is passed on to consumers.
- These energy shocks highlight India's **external sector vulnerability** and **energy insecurity**.

4. Inflation Outlook and Monetary Policy Stability

- **Retail inflation (CPI)** dropped to **2.82% in May**, the **lowest in over six years**, mainly due to softening **food prices**.
- RBI remains confident of **inflation aligning durably** with its **medium-term target of 4% (+/- 2%)**, giving the central bank **monetary policy flexibility**.
- This **sub-4% inflation streak for four consecutive months** is the **longest in five years**, providing relief amid global uncertainties.



5. Institutional and Global Perspectives on Growth

- International organizations like the **IMF, OECD, and World Bank** have **revised global growth projections downward**, reflecting rising **policy uncertainty**.
- The **spillover effects** of global economic shifts necessitate **vigilant macroeconomic management** by Indian authorities.



Key Definitions & Legal Framework

- **Consumer Price Index (CPI):** Measures changes in the price level of a basket of consumer goods and services.
- **Monetary Policy Framework Agreement (2016):** Empowers RBI to maintain **CPI inflation at 4%**, with a tolerance band of **+/-2%**.
- **Current Account Deficit (CAD):** When a country's imports of goods/services exceed exports.
- **Financial Stability Report (FSR):** A biannual publication by the RBI assessing risks to India's financial system.

Conclusion

India's economic resilience is currently being tested by **external challenges**—ranging from **protectionist trade policies** and **geopolitical shocks** to **climate-related disruptions**. While **inflation remains benign** and **domestic fundamentals strong**, the **spillover from global uncertainties** could impact growth and financial stability. Policymakers must balance **external risk management**, **energy security**, and **trade diplomacy**, while leveraging **domestic reforms** to sustain growth in an unpredictable global environment.

3. India Reassesses Key Digital and Trade Laws Amidst US Pact Negotiations

1. India-US Trade Pact Spurs Review of Key Domestic Policies

- As India nears a **bilateral trade agreement with the US**, it is reassessing several **pending domestic legislations and policy frameworks** that affect American tech companies.
- The review includes the **Digital Competition Bill**, the **e-commerce policy**, and **profit attribution rules** for non-resident enterprises under the Income Tax Act.
- These changes are aimed at aligning Indian laws with global norms and **creating a trust-based investment climate**, potentially using them as **negotiation tools** in trade discussions.

2. Digital Competition Bill: Regulating Big Tech

- The proposed **Digital Competition Bill** is a forward-looking measure to regulate **dominant digital platforms**, mandating them to follow a **code of conduct**.
- It targets practices like **targeted advertising**, **data use**, and **preferential treatment of services** by large firms like Google and Meta.
- The Bill may be delayed or altered in light of trade discussions, to avoid friction with the US.

3. Taxation of Digital Services and SEP Rules

- India has **removed the Equalization Levy**, which was earlier imposed on digital services provided by foreign firms, to ease tensions with the US and align with **OECD's BEPS (Base Erosion and Profit Shifting) framework**.





- However, India still retains the **Significant Economic Presence (SEP)** concept and **draft profit attribution rules** under **Section 9 and Rule 10** of the **Income Tax Act**, which aim to tax foreign firms based on user base and transaction volume—even without a **Permanent Establishment (PE)**.
- These rules remain under review, and have not yet been enforced.

4. E-commerce Policy and FDI Reforms Under Scrutiny

- India's **comprehensive e-commerce policy**, which seeks to regulate digital marketplaces, is being reconsidered due to global geopolitical sensitivities.
- A **revision in FDI rules for retail**, allowing foreign players to hold inventory (currently restricted), is also being evaluated to attract investment and balance trade interests.

5. Strategic Importance and Policy Leverage

- India's approach to digital and trade laws is now being seen as a **lever in bilateral negotiations**.
- According to experts, the **timing and framing of these laws** can be used to negotiate favorable terms in the **India-US trade agreement**, while ensuring **policy predictability and investor confidence**.
- India must strike a balance between **domestic regulatory sovereignty** and **global economic engagement**.

Key Definitions & Legal Context

- **Equalization Levy:** A tax on digital services provided by foreign e-commerce firms, now withdrawn.
- **Significant Economic Presence (SEP):** A legal concept under Section 9 of the **Income Tax Act** to tax foreign companies with large user bases or digital transactions in India.
- **Permanent Establishment (PE):** A fixed place of business through which a foreign enterprise conducts business, triggering taxation rights under tax treaties.
- **Digital Competition Bill:** A proposed Indian law to regulate anti-competitive practices in the digital economy, promoting fair digital markets.

Conclusion

India's recalibration of critical policy instruments in the digital and taxation space reflects a **strategic shift in its global trade engagement**, particularly with the US. While protecting **sovereign regulatory space**, India seeks to enhance its **investment climate** and **digital economy governance**.

4. April–May Fiscal Deficit Hits Record Low Amid Surge in Non-Tax Revenue

1. Record Low Fiscal Deficit in April–May FY26

- India's fiscal deficit for April–May 2025-26 stood at \square 13,163 crore, or 0.8% of the full-year target, the lowest since 1997, when monthly fiscal data reporting began.



- In comparison, the fiscal deficit during the same period in FY25 was ₹50,615 crore.
- This reflects strong **fiscal consolidation** efforts and improved revenue inflows despite rising expenditure.

2. Significant Growth in Non-Tax Revenue

- **Non-tax revenue surged to ₹3.57 trillion**, accounting for **61.2% of the annual estimate**, aided mainly by:
 - A record **₹2.69 trillion dividend** from the **Reserve Bank of India (RBI)**.
 - Proceeds from **asset monetization** and **disinvestment** (non-debt capital receipts).
- This compensated for the relatively **slower tax revenue growth**, which stood at ₹3.51 trillion (12.4% of FY target).

3. Capital Expenditure Front-Loaded

- The government pushed capital outlay to ₹2.21 trillion (19.7% of full-year target) during April–May FY26, up from ₹1.44 trillion in FY25.
- The boost comes after capital spending slowed in Q1 FY25 due to general elections, indicating a focus on **infrastructure-led growth**.
- **Overall expenditure** rose to ₹7.46 trillion (14.7% of annual estimate), with **revenue expenditure** at ₹5.25 trillion (13.3%).

4. Fiscal Deficit Target and Long-Term Strategy

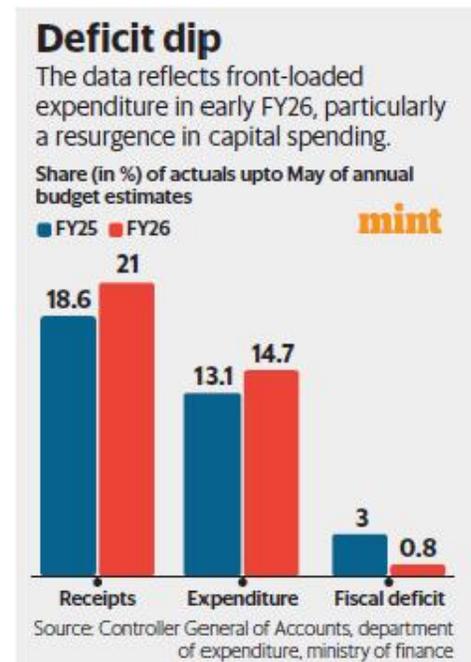
- The fiscal deficit for FY26 is projected at ₹15.69 trillion, or **4.4% of GDP**, down from ₹16.85 trillion in FY25.
- The government remains committed to the **Fiscal Responsibility and Budget Management (FRBM) Act** glide path to achieve long-term **fiscal sustainability**.
- A potential **shift from fixed-point fiscal targets to a range-based approach (3.7–4.3%)** beyond FY26 is under consideration to enhance **policy flexibility**.

5. Definition and Importance of Fiscal Deficit

- **Fiscal Deficit = Total Expenditure – (Revenue Receipts + Non-Debt Capital Receipts)**
- It represents the **gap between government income and spending**, indicating the **amount to be borrowed**.
- Moderate deficits are acceptable to support growth, but excessive ones can lead to **inflation** and rising **public debt**.

Key Constitutional & Legal Context

- **Article 112** of the Constitution: Provides for the **Annual Financial Statement (Union Budget)**.





- **FRBM Act (2003):** Mandates fiscal discipline by limiting fiscal and revenue deficits and ensuring **intergenerational equity**.
- **Controller General of Accounts (CGA):** Publishes monthly fiscal data and monitors government accounts.

Conclusion

India's sharp drop in fiscal deficit during the first two months of FY26 is a **positive macroeconomic signal**, showcasing improved **revenue mobilization**, especially from **non-tax sources** like RBI dividends. The government's adherence to **capital expenditure** targets while maintaining **fiscal prudence** reflects a **balanced growth strategy**. Going forward, a range-based fiscal targeting mechanism may help address **economic uncertainties** while ensuring **sustainable public finance**.

5. Retired Coal Plants Eyed for Nuclear Use

1. Strategic Repurposing of Retired Coal Plants

- The Government of India is exploring the **conversion of retired coal-based power plants** into **nuclear power plants**, to overcome land scarcity and accelerate nuclear capacity expansion.
- This initiative aligns with the target of installing **22 GW of nuclear capacity by 2032** and **100 GW by 2047**, up from the current **8.78 GW**.

2. Land and Infrastructure Optimization

- **Nuclear power plants** require **large contiguous land parcels**, which are difficult to acquire.
- Retired coal plants offer:
 - **Existing land availability**
 - **Pre-established transmission and evacuation infrastructure**
 - **Water access**
 - **Grid connectivity**
- According to a **US Department of Energy (2022)** report, **repurposing thermal plants** can save up to **35% in project costs**.

3. Grid Stability and Base Load Concerns

- Despite India's push for **renewable energy**, **coal still forms the backbone** of India's power system (212.71 GW out of 472.46 GW installed capacity).
- **Nuclear power**, while non-renewable, is **low-carbon** and contributes to **base-load generation** and **grid stability**, similar to coal, unlike intermittent sources like wind and solar.

4. Current Nuclear Capacity and Future Pipeline

- India operates **25 nuclear reactors across 7 locations**, generating about **3% of national electricity**.



- **14.3 GW of nuclear capacity** is in various stages of implementation, with **7.3 GW under construction**, according to the Ministry of Power.

5. Regulatory and Safety Considerations

- Conversion of coal plants to nuclear use requires:
 - **Rigorous feasibility studies**
 - **Environmental and safety clearances**
 - Compliance with the **Atomic Energy Act, 1962** and rules laid by the **Atomic Energy Regulatory Board (AERB)**.
- The Centre has asked states to **identify and plan at least one nuclear plant**, encouraging decentralized participation.



Key Definitions & Legal Framework

- **Nuclear Energy**: Energy released during nuclear fission or fusion, used for electricity generation.
- **Base-load Power**: The minimum level of demand on an electrical grid over a span of time; best supported by stable sources like coal or nuclear.
- **Atomic Energy Act, 1962**: Governs all nuclear energy production and research in India, empowering the **Department of Atomic Energy (DAE)**.
- **AERB (Atomic Energy Regulatory Board)**: Ensures safety regulations and radiation protection in India's nuclear installations.

Conclusion

The proposed **conversion of retired coal power plants into nuclear facilities** presents a **cost-effective and time-efficient** strategy to ramp up India's **clean and stable energy** capacity. It leverages existing infrastructure while supporting India's **energy transition goals** under the broader climate commitments (like Net Zero by 2070). However, such conversions will require **careful regulatory scrutiny**, environmental safety, and public trust, making this an important development for energy security, federal coordination, and sustainable growth

6. Eight Years of GST: A Milestone in Indirect Tax Reform

1. GST Strengthens Ease of Doing Business

- Introduced on **1st July 2017**, the **Goods and Services Tax (GST)** subsumed multiple indirect taxes, creating a **unified national market**.
- As per the Finance Ministry, GST has significantly improved the **ease of doing business**, especially for **Micro, Small and Medium Enterprises (MSMEs)** by:
 - Simplifying tax compliance.



- Enabling easier **access to credit**, especially via the **Trade Receivables Discounting System (TReDS)**.

2. Revenue Growth and Taxpayer Base Expansion

- **GST revenues have nearly doubled:** from ₹11.37 trillion in FY21 to ₹22.08 trillion in FY25.
- Over **15 million taxpayers** are now registered under GST, reflecting broader **economic formalization and compliance**.
- The system has leveraged **digital tools** for real-time invoice matching, e-way bills, and improved tax enforcement.

3. Ongoing Reforms in GST Architecture

- The government is working on **rationalizing GST rate slabs**, with proposals to merge the **12% slab with either the 5% or 18%**.
- This aims to **correct anomalies** such as **higher taxes on raw materials than on finished goods**, reducing the problem of **inverted duty structure**.



4. Improved Credit Access Through TReDS

- **TReDS (Trade Receivables Discounting System)** enables MSMEs to **sell unpaid invoices** to banks/NBFCs, improving **working capital liquidity**.
- Over **5,000 buyers**, **53 banks**, and **13 NBFCs** are currently participating in the TReDS ecosystem.

5. Challenges and Next Steps in GST Evolution

- As noted by **PricewaterhouseCoopers**, the next phase must focus on:
 - **Simplification** of tax rates and procedures.
 - **Unblocking tax credits**, particularly in sectors affected by the inverted duty structure.
 - **Operationalizing GST Appellate Tribunals** for quicker dispute resolution.
 - **Stabilizing tax policy** to build industry trust and reduce litigation.

Key Definitions & Legal Provisions

- **GST (Goods and Services Tax):** A **destination-based, value-added tax** on the supply of goods and services.
- **Article 246A** of the Constitution: Empowers both Parliament and State Legislatures to make laws on GST.
- **GST Council (Article 279A):** A constitutional body chaired by the Union Finance Minister that recommends GST rates and policies.
- **TReDS:** RBI-regulated platform to finance trade receivables of MSMEs from corporate buyers.



Conclusion

In its **eight-year journey**, GST has transformed India's indirect tax landscape by **integrating markets**, **boosting compliance**, and **empowering MSMEs**. However, the system now needs a **second generation of reforms**—especially in **rate rationalization**, **credit refunds**, and **dispute resolution**—to make it **simpler**, **more stable**, and **more inclusive**. For UPSC aspirants, GST exemplifies **cooperative federalism**, **tax reform**, and the role of **digital governance** in economic policy.

7. Small Savings Scheme Rates Unchanged for July–September FY26

1. Interest Rates on Small Savings Schemes Kept Unchanged

- The **Ministry of Finance** has decided to **maintain the existing interest rates** on all **small savings schemes** for the **July–September quarter of FY26**.
- This move comes amid **stable inflation trends** and **steady yields on government securities**.

2. What are Small Savings Schemes?

- **Small Savings Schemes** are **government-backed saving instruments** that offer fixed interest and tax benefits, and are popular among the middle class, senior citizens, and rural households.
- Key schemes include:
 - **Public Provident Fund (PPF)**
 - **National Savings Certificate (NSC)**
 - **Senior Citizen Savings Scheme (SCSS)**
 - **Sukanya Samridhi Yojana**
 - **Kisan Vikas Patra (KVP)**
 - **Monthly Income Account Scheme (MIS)**
 - **Time Deposits and Recurring Deposits**



3. Basis for Interest Rate Fixation

- Interest rates on small savings schemes are **linked to government securities (G-secs)** of comparable maturity.
- As per the **Shyamala Gopinath Committee (2011)** recommendations, rates are revised **quarterly** based on a spread over G-sec yields.

4. Economic Context and Policy Stability

- Keeping rates unchanged reflects the government's **balanced approach to managing returns and borrowing costs**.
- It ensures **predictability for investors**, especially in a period of **moderate inflation** and **stable macroeconomic conditions**.



5. Constitutional and Legal Framework

- While not directly mentioned in the Constitution, small savings fall under the **Union List Entry 43** (Loans raised for the Union Government).
- They are managed by the **National Small Savings Fund (NSSF)** under the **Public Account of India** as per provisions of the **Government Accounting Rules**.

Conclusion

By keeping the **small savings scheme interest rates unchanged** for Q2 FY26, the government aims to **preserve investor confidence and maintain economic stability**. These schemes continue to play a vital role in **financial inclusion, household savings mobilization, and non-market borrowing** by the government.

8. RBI Reduces Short Dollar Positions in Forward Market

1. RBI Cuts Short Dollar Positions to \$65.2 Billion

- The **Reserve Bank of India (RBI)** has reduced its **net short dollar positions** in the **foreign exchange forward market** to **\$65.2 billion as of May 2025**, down from **\$72.6 billion in April** and **\$88.8 billion in February**.
- This is the **third consecutive monthly reduction**, indicating a **strategic shift in forex intervention** under new RBI Governor **Sanjay Malhotra**.

2. What Are Short Dollar Forward Positions?

- In the **forex derivatives market**, a **short dollar position** implies the central bank has sold more dollars forward than it has bought.
- It's often used as a tool to **manage rupee volatility** without directly affecting spot reserves.
- This can **delay the impact** of forex interventions on the actual reserves but may increase **foreign exchange (FX) liabilities** in the future.

3. Strategy to Reduce Forex Vulnerability

- The RBI's move is aimed at **mitigating foreign exchange risks** by reducing large **near-term dollar outflows**.
- Currently:
 - **\$30 billion** is due in the **3-month to 1-year bucket**
 - **\$20.1 billion** lies in the **more than one-year maturity segment**, mostly from **buy/sell swaps**.

4. Role of Buy/Sell Swaps

- **Buy/sell swaps** are derivative contracts used by RBI to **buy dollars and sell them forward**, helping:





- Stabilize the rupee
- Manage liquidity in the banking system
- Offset temporary market pressures without impacting spot reserves

5. Constitutional & Legal Framework

- The RBI's actions are guided by:
 - **RBI Act, 1934** – which empowers RBI to regulate foreign exchange and intervene in currency markets.
 - **Foreign Exchange Management Act (FEMA), 1999** – which governs foreign exchange transactions and external sector policy.
- These laws empower RBI to **maintain external stability, manage reserves, and stabilize the rupee.**

Conclusion

RBI's gradual reduction in short dollar forward positions reflects a **calibrated strategy to reduce FX market vulnerability** and ensure **external sector stability**. For UPSC aspirants, this showcases how **central banks use derivative tools** to influence currency markets, while balancing **foreign exchange reserve adequacy, external debt management, and monetary policy goals**.

9. RBI Projects Marginal Rise in Bank NPAs by FY27

1. Gross NPAs Likely to Rise Slightly by FY27

- As per the **RBI's Financial Stability Report (FSR)**, the **Gross Non-Performing Assets (GNPA) ratio** for 46 major banks may rise **from 2.3% in March 2025 to 2.5% by March 2027** under the **baseline stress scenario**.
- The **GNPA ratio** is a key indicator of asset quality, reflecting the percentage of loans that have turned bad.

2. Adverse Scenarios Could Push NPAs Above 5%

- Under **Adverse Scenario 1** (Geopolitical Risk Scenario), GNPA may rise to **5.6%**.
- Under **Adverse Scenario 2** (Global Slowdown Scenario), GNPA may increase to **5.3%**.
- Both scenarios simulate shocks from **global financial volatility, supply chain disruptions, and economic slowdown**.

3. Capital Buffers Remain Adequate

- Even in stress conditions, **Capital to Risk-Weighted Assets Ratio (CRAR)** remains **above the regulatory minimum of 9%**:
 - **17% (baseline)**



- **14.2% (adverse scenario 1)**
- **14.6% (adverse scenario 2)**
- **Common Equity Tier I (CET-1) ratio**, which reflects high-quality core capital, also stays above the minimum required **5.5%**, ensuring resilience.

4. Stress Testing Methodology Explained

- RBI stress tests evaluate banks' strength under three scenarios:
 - **Baseline**: Based on expected macroeconomic indicators.
 - **Adverse 1**: High geopolitical risk and inflation.
 - **Adverse 2**: Global recession and lower growth spillovers.
- Stress tests assess risks from **credit defaults, market instability, and liquidity shocks**.

5. Credit Concentration Risk and Systemic Stability

- Stress test on **top 3 individual and group borrowers' default** shows:
 - System-level CRAR could decline by **90–130 basis points**.
 - However, **no bank's CRAR falls below 9%**, though **4 banks may see a fall of more than 2%**.
- This highlights the importance of **diversifying lending portfolios** and **managing large borrower exposures**.

Key Legal & Regulatory Provisions

- RBI's oversight is enabled by:
 - **Banking Regulation Act, 1949**
 - **RBI Act, 1934**
 - **Basel III Norms**: International standards for bank capital and liquidity
 - **Section 35A** of the Banking Regulation Act empowers RBI to conduct inspections and impose corrective action.

Conclusion

The RBI's stress test results reflect **robustness in the Indian banking system**, with **limited rise in NPAs and adequate capital buffers** under both expected and adverse economic scenarios.

10. India's AI Push and GPU Procurement: A Gamechanger for Cloud and Digital Infrastructure

1. India AI Mission Boosts Cloud Infrastructure Sector



- The **India AI Mission**, launched with a budget of **\$1.2 billion**, is significantly boosting **domestic cloud service providers** like Reliance Jio Platforms, Tata Communications, and Yotta Data Services.
- The mission focuses on building a **central compute infrastructure** by **procuring over 34,000 GPUs (Graphics Processing Units)**, which are vital for AI model training and large-scale data processing.

2. Role of GPUs in AI Ecosystem

- **GPUs** are specialized processors that perform complex parallel computations, crucial for **AI model development**, such as **Natural Language Processing (NLP)** and **Computer Vision**.
- Government procurement has enabled startups (e.g., **Sarvam, Gnani.ai, Soket AI Labs**) to access this infrastructure, enhancing India's capacity to build **foundational AI models**.



3. Revenue Growth for Indian Cloud Firms

- Companies like **Yotta** and **Tata Communications** are witnessing exponential growth:
 - Yotta is supplying nearly **17,000 GPUs**, expecting **70% revenue** from government orders.
 - Tata Communications saw **13% growth in cloud services**, with 42% of its total revenue now from India.
- These firms are capitalizing on both **government-backed and enterprise AI demand**.

4. Strategic Government Intervention

- The **Ministry of Electronics and Information Technology (MeitY)** leads GPU procurement under the AI Mission.
- **First Tranche (Jan 2025)**: 18,693 GPUs.
- **Second Tranche (May 2025)**: 15,640 GPUs.
- This has created India's **first centralized AI compute infrastructure**, fostering long-term, production-grade AI projects.

5. Challenges: Red Tape and Procurement Hurdles

- Analysts caution against bureaucratic inefficiencies and restrictive tendering processes that may slow implementation.
- Addressing these issues is critical to fully realize the AI Mission's potential and scale up **Make-in-India digital infrastructure**.



Key Terms & Legal Context

- **GPU (Graphics Processing Unit)**: A parallel processing unit designed to accelerate graphic rendering and complex computations.



- **India AI Mission:** A centrally-funded digital initiative aiming to develop India's AI capabilities, announced in 2023-24.
- **Digital India Programme:** An umbrella programme by the **Ministry of Electronics and IT** (under **Article 73**) aiming for digital empowerment of citizens and infrastructure development.
- **Public Procurement Policies** under the **General Financial Rules (GFR), 2017**, govern how government tenders and technology procurement are done.

Conclusion

India's AI Mission is a pivotal initiative driving rapid **technological advancement, cloud infrastructure development, and digital innovation**. By integrating state-backed GPU procurement with private sector innovation, India is positioning itself as a **global AI hub**.

II. India's Strategic Compass in a Perilous World: Rethinking Foreign and Security Policy

1. India's Neutrality Challenged Amid Global Realignments

- India's traditional **non-aligned and balanced diplomacy**, especially between rival blocs (e.g., Israel-Iran, US-China), is increasingly ineffective in the current geopolitical climate.
- The **Israel-Iran conflict**, with US support for Israel using GBU-57 bunker-buster bombs, has escalated tensions, making neutrality risky.
- India's muted stance has cost it diplomatic leverage, particularly with Iran, weakening its claim as a moral leader of the **Global South**.

2. China-Pakistan Axis: A Growing Threat

- India must urgently reassess the **China-Pakistan military nexus**, especially following reports of Chinese equipment and strategic integration into Pakistan's defence plans.
- Joint capabilities such as **JF-17 and J-10C fighter jets**, missile systems, and potential nuclear coordination threaten India's preparedness for a **two-front war**.
- China's latest white paper on "**National Security in the New Era**" emphasizes securing supply chains and technological self-reliance, signaling growing regional militarization.

3. U.S. Foreign Policy and its Implications for India

- Under the '**America First**' and **MAGA** doctrine, U.S. policy is increasingly transactional, sometimes undercutting India's position—as evident in Trump's claims of mediating the India-Pakistan conflict.
- India's refusal to engage in certain diplomatic overtures (e.g., skipping Trump's invitation post-G7) risks





alienation in the Indo-Pacific calculus, despite shared goals of countering China.

4. Erosion of Moral Diplomacy and Rise of Hard Power

- Global diplomacy now favors **realpolitik and military alliances** over consensus or morality—seen at the **Shangri-La Dialogue**, where the US-China rivalry dominated.
- **Soft power**, long a pillar of India's foreign policy, must now be augmented by **hard power capabilities**, including **cyber, electromagnetic warfare, and AI-based defense systems**.

5. India's Strategic Gaps and Need for Defense Reforms

- India must reassess its preparedness for **long-duration or high-intensity conflicts** by:
 - Conducting audits of **ammunition and logistics** reserves.
 - Establishing **National Armament Systems and Cyber/Electromagnetic Commands**.
 - Prioritizing **drone warfare, AI, loitering munitions, and glide bombs** to modernize its forces.
- Lessons from **Russia-Ukraine War** are critical in shaping India's strategic outlook.

6. Nuclear Asymmetry Must Be Acknowledged

- The open mention of the '**N-word**' (**nuclear weapons**) in international discourse signals a shift towards brinkmanship.
- India faces a **nuclear disadvantage**: China holds a 3:1 edge in nuclear warheads, and when combined with Pakistan, the ratio rises to **5:1**, necessitating strategic recalibration.

Key Concepts for UPSC

- **Non-alignment**: A diplomatic stance of not aligning with any power bloc; India was a founding member of the **NAM (Non-Aligned Movement)**.
- **Strategic Autonomy**: India's foreign policy goal of pursuing national interest without undue influence from any global power.
- **Two-Front War Doctrine**: India's military planning concept of simultaneous conflict with **Pakistan on the west and China on the east/northeast**.
- **Comprehensive National Power (CNP)**: A nation's combined military, economic, technological, and diplomatic strength.

Conclusion

In a rapidly changing and perilous global order, **India's traditional policy prescriptions—non-alignment, moral diplomacy, and strategic ambiguity—require urgent rethinking**. With **rising regional hostilities, a China-Pakistan military alignment**, and an erosion of soft power relevance, India must invest in **military modernization, strategic alliances, and internal defence reforms**. Reading the "**geopolitical tea leaves**" correctly will be vital for safeguarding India's sovereignty, regional influence, and global standing.



12. GST Reform and the Unfinished Agenda in Tobacco Taxation

1. GST as a Landmark Economic Reform

- **Goods and Services Tax (GST)** was launched on **1 July 2017**, replacing multiple indirect taxes (e.g., VAT, excise, service tax), creating a **unified national tax framework** under "One Nation, One Tax".
- It simplified tax compliance, reduced cascading taxes via **Input Tax Credit (ITC)**, improved logistics efficiency (e.g., reduced transportation time by 20%), and digitized administration (e.g., e-way bills).
- GST collections reached **₹22.08 lakh crore in FY25**, indicating strong revenue growth (9.4% YoY).

2. Tobacco Taxation: A Public Health and Fiscal Paradox

- **Tobacco-related diseases** cause over **3,500 deaths daily** and impose an economic burden of **₹2.34 lakh crore annually (1.4% of GDP)**.
- However, GST revenue from tobacco remains around **₹55,100 crore annually**, far less than its health costs.
- India's **overall tax burden on tobacco products** (22% for bidis, 54% for cigarettes, 65% for smokeless tobacco) falls short of **WHO's recommended 75%**.



3. Flaws in the Current Tax Design

- Post-GST, India shifted to predominantly **ad valorem taxation** (percentage of price), reducing the share of **specific excise duties**, which are more effective at reducing consumption.
- For example, excise duty share fell from:
 - 54% to 8% for cigarettes,
 - 17% to 1% for bidis,
 - 59% to 11% for smokeless tobacco.
- Bidis, despite being **the most consumed tobacco product**, are **not subject to the GST compensation cess**, making them highly affordable and under-taxed.

4. The Issue of GST Compensation Cess Expiry

- The **GST compensation cess**, a major component of tobacco tax, is set to expire by **March 2026**.
- If not extended or replaced, this will reduce total taxation on tobacco, making it more affordable and undercutting public health goals.
- **GST law permits raising tobacco product tax rates to 40%**, providing legislative space for corrective action.



5. Addressing Illicit Trade: Myth vs Reality

- Tobacco industry claims that higher taxes fuel **illicit trade**, but studies show illicit cigarette market share in India is only **2.7%–6.6%**, not 25% as claimed.
- Illicit trade is more influenced by **regulatory enforcement and governance quality**, not taxation alone.
- India has **ratified the WHO Protocol to Eliminate Illicit Trade in Tobacco Products** and must focus on its effective implementation.

Key Concepts for UPSC

- **Ad valorem tax**: Tax based on the value of goods (e.g., GST).
- **Specific excise duty**: Fixed tax per unit (e.g., ₹100 per pack), more effective in discouraging harmful product use.
- **Input Tax Credit (ITC)**: A mechanism to reduce tax cascading by allowing credit on inputs used for producing goods/services.
- **GST Compensation Cess**: Additional cess levied on luxury and sin goods (like tobacco) to compensate states for GST revenue loss.

Conclusion

The eighth anniversary of GST presents a strategic opportunity to **reform the taxation structure on tobacco products**. By **raising GST rates to the statutory peak of 40%** and **reviving or increasing specific excise duties**, India can meet its **public health obligations**, align with **WHO norms**, and ensure **fiscal consolidation**. The GST Council's ongoing **rate rationalisation** must prioritize **public health objectives** alongside economic goals, making GST not just a revenue tool, but a powerful instrument for **nation-building and health policy**.