Stumbling blocks in arbitration

Longstanding maladies plague this disputes resolution mechanism; law alone cannot make it attractive

OUT OF COURT

M J ANTONY

The government, corporations and the legal profession have been trying hard over decades to make India attractive as an arbitration centre. But London, Singapore and other foreign hubs continue to be cited in contracts as prime choices. There are several reasons for this, like inadequate infrastructure facilities here, uncertainty in laws, unconscionable delays and ambiguous judicial pronouncements. The New Delhi International Arbitration Centre Bill 2018 was passed by the Lok Sabha a year ago to remedy some of these but is not likely to be in force too soon.

Meanwhile, a glance at the judgments delivered by the Supreme Court and high courts points to some serious deficiencies in the arbitration process, despite significant changes made in the Arbitration and Conciliation Act in 2015. The appeals which reach the apex level are symptomatic of the problems.

One recurring point of discord is the choice of arbitrators. The SC has written several judgments against compulsorily making bureaucrats and officials of public sector enterprises as arbitrators in their own causes, but the practice continues. Though the amended law has two schedules barring certain persons acting as arbitrators, this issue is often the first hurdle. The parties wrangle over the choice of the arbitrator, casting doubts over his independence and impartiality. The courts have not cleared the confusion over it.

"The fact that an arbitrator is an employee of one of the parties is not by itself a ground to raise a presumption of bias or lack of independence on his part," the SC stated in its judgment, Sp Singla Constructions vs State. The court has ruled that an engineer retired from the Public Works Department can act as an arbitrator in a dispute between the department and a contractor (PWD Haryana vs GF Toll Road Ltd). On the other hand, the Jharkhand high court observed in a case that leaving a private firm at the mercy of officials against whom claims are made would add insult to injury and affect the credibility and impartiality of the whole process (Sahil Projects vs Eastern Railway).

There is no reservoir of professionals trained in the art of arbitration. So the choice falls on retired judges. The SC has observed in a judgment that such judges are not only costly but also tend to drag the process. One session ends by deciding the date for the next meeting at another posh venue. A few weeks ago, one retired judge was disqualified by the Rajasthan high court as he demanded ₹75 lakh for accepting the assignment.

The conduct of the parties, especially government entities sitting on huge litigation funds, has received acerbic remarks. The Delhi high court imposed heavy fine on National Highways Authority of India (NHAI) for rendering "yeoman disservice" to the object of the Act. In another NHAI case, the court wrote: "We find this court inundated by challenges against arbitral awards by PSUs seeking re-appreciation of the findings of the arbitrator. Such litigation defeats the very purpose of the Act."

It is not uncommon to find government entities fighting each other in arbitration. The SC efforts to stop such fratricidal battles failed years ago. An oversight committee of the government to stop the urge to splurge public money on futile litigation has wound up, leaving government arms free to hold each other by the throat.

Delays in the arbitration give the process a bad name. In one case, Essel Infra Projects Ltd was frustrated by delays and sought SC help to speed up the process. But it only prescribed non-mandatory suggestions.

The court appointed a new umpire in a two-decade old tax dispute between Hyundai and ONGC.

Legalese can also suspend the process. A dispute on the interpretation of 'venue' and 'seat' of arbitration has been referred to a larger bench by the SC. Most of us believe that top lawyers who draft contracts would leave no loopholes in contracts. But judges have been made to search for an arbitration clause in several agreements. They discover it in oral assurances and correspondence between the parties and unsigned documents.

These are specimens which highlight what ails arbitration. There are rows of them. The proposed Bill has touched upon the theoretical aspects but even if it is passed it cannot tackle the problems at the level of implementation.

CHINESE WHISPERS

Election season

PIC: MANAVI KAPUR

As the gathering of non-resident Indians, persons of Indian origin and foreign nationals at the Pravasi Bharatiya Divas in Varanasi waited for Prime Minister Narendra Modi to arrive, the emcee of the event welcomed the foreign delegates and urged them to be seated. In one of her announcements, she also urged visitors to download the NaMo app — a mobile application handled by the Bharatiya Janata Party. The app, she said, could be downloaded from special digital booths at the venue, which in turn stood beside a photobooth to click selfies with a virtual cutout of the prime minister. Election season seems to be officially open.

Fact or fiction?

Prime Minister Narendra Modi is not the only one talking about the government's initiatives on air. The government has roped in veteran author, lyricist and scriptwriter Neelesh Misra to narrate the experiences of young people who have benefitted from the Skill India initiative. A programme titled *Inn Haathon Se Bann Raha Bharat* is set to air twice a week on a private radio station. However, the officials at the Ministry of Skill Development and Entrepreneurship did not clarify if the stories would be based on real people, or would be mere works of fiction, as Misra's many other tales usually are.

Chasing cows

Stray cows and bulls have become quite a menace in large parts of northern India, particularly Uttar Pradesh. Varanasi, the venue of this year's Pravasi Bharatiya Divas, has always had its share of stray cows. In the run up to the event, Uttar Pradesh Chief Minister Yogi Adityanath had instructed the local administration to prevent stray cows from sauntering inside the sprawling venue. However, a cow entered the makeshift venue on Tuesday afternoon when Prime Minister Narendra Modi was inside the auditorium for the opening ceremony of the event. Fortunately, the cops could chase the docile animal away without much effort.

The 'blue flame' revolution

Why the government can unambiguously take credit for the scheme to distribute cooking gas to poor rural households

SHINE JACOB

TAKE TWO

"Due to bad figures in PMUY [Pradhan Mantri Ujjwala Yojana] during past week, kindly suspend all domestic LPG supply to this gas agency".

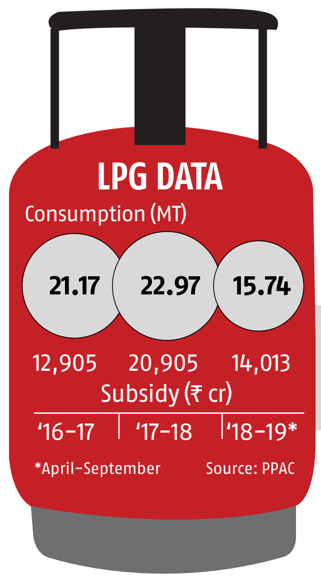
This is an excerpt from a letter written by an LPG sales officer of an oil marketing company (OMC) about a gas agency in Uttar Pradesh's Rampur in October 2016. The letter, written just five months after the ambitious Pradhan Mantri Ujjwala Yojana (PMUY) scheme was launched at Balia in May 2016, reflected the "perform or perish" diktat that Narendra Modi attached to his "blue flame revolution," to transform the lives of millions of housewives in rural India.

In a country where the best plans trip on implementation, this hard-line approach has worked. Liquefied petroleum gas (LPG) penetration increased from 62 per cent in 2016 to 90 per cent now, PMUY accounting for almost half this increment. As on January 18, the plan to distribute free cooking gas connections to poor households of state-owned OMCs — Indian Oil Corporation (IOC), Bharat Petroleum Corporation (BPCL) and Hindustan Petroleum Corporation (BPCL) — covered 61.2 million consumers in 715 districts.

LPG connections were initially provided to women in Below Poverty Line (BPL) families with a support of Rs 1,600 per connection for the stove and first refill; in December 2018, its ambit was expanded to "all-poor," which means those who do not fall within various government-identified lists. Under this, IOC alone has extended Rs 3,125 crore as loans that allow beneficiaries to repay based on their convenience till the next six refills, of which Rs 955 crore has been repaid.

The scheme owes it success to the daily monitoring by petroleum minister Dharmendra Pradhan and officials at joint secretary and director level, an OMC official confirms. He recalled the example of a norther district nodal officers' meet in Lucknow last year. "The minister named each of 200-odd officials by name and, much to our surprise, we learnt that he used to make phone calls to them to boost their morale. Such minor things helped PMUY," he said.

The importance of good implementation can be seen in the contrasting performance of a version of the scheme under prime minister Manmohan Singh's United Progressive Alliance (UPA). Indeed, the idea of subsidising cooking gas for poor rural households was mooted during the UPA's second stint. Labelled the Rajiv Gandhi Gramin LPG Vitaran (RGGLV) scheme, it was launched in 2009.



UJJWALA YOJANA

LAUNCH
May 1, 2016 at Ballia, UP

TARGET
Providing LPG to BPL families with a support of ₹1,600 per connection

TOTAL CONNECTIONS PROVIDED
61.2 million (till January 21, 2019)

INCREASE IN LPG PENETRATION SINCE PMUY
From 62 per cent in 2016 to 90 per cent now

RISE IN NUMBER OF DISTRIBUTORS
Number of LPG consumers increased by 60.6 per cent in four years from 13,896 in March 2014 to 22,328 in November 2018

NUMBER OF CONSUMERS (MILLION)

Indian Oil	HP	BP
118	69	64

HP: Hindustan Petroleum; BP: Bharat Petroleum
SOURCE: MoPNG

This scheme was discontinued by the National Democratic Alliance for almost a year before it re-emerged as PMUY. The erstwhile scheme also focused on mobilising distribution through dealer networks but in five years only 4,000 new domestic cooking gas distributors were added. Over the past four years, the number of LPG distributors increased 60.6 per cent from 13,896 in March 2014 to 22,328 in November 2018 (all of them servicing PMUY).

Still, PMUY faces its challenges. Ironically, usage frequency is one of them. The average refill by a PMUY consumer is 3.28 cylinders a year against seven by a normal consumer. Affordability is one factor, since a cylinder costs Rs 689, even touching Rs 942.5 in November 2018.

Responding to a query on Twitter, Ashutosh Jindal, joint secretary-marketing, in the petroleum ministry, said, "Refills are an issue for some poor households which we are trying to address through 5 kg refills and by setting up points of delivery." This enables PMUY beneficiaries to swap a standard 14.2 kg cylinder with a 5 kg refill. As on December 31, 2018, less than one per cent of the PMUY beneficiaries had availed of this option.

"The intensity of demand and affrdability in rural India is expected to be low. Getting the LPG-use mindset and supply chain in place will take months and years," Deepak Mahurkar, partner and leader — oil & gas industry — PwC India, pointed out.

Jindal says complete conversion to LPG as a cooking fuel has socio-economic and behavioural dimensions. "Some alternative fuels like cow dung, firewood may be completely free of cost for a rural household. It will take time for a family to appreciate that what seems to be free has other costs like health impact, time lost, which could have been used for productive livelihood," he said.

OMCs' efficiency in LPG distribution is also an issue, because greater penetration increased pressure on LPG bottling plants. The 190 bottling plants in the country now run at over 120 per cent capacity utilisation. The slow pace in getting clearances for bottling units is adding to the problems.

To tackle the issue, companies are planning to set up 60 such units across the country at an investment of Rs 400 crore. "The sector also needs reforms to bring in supply chain efficiency to reduce the costs that are passed on to consumers. Public sector companies have the strength to make the fuel reach remote and far-flung areas. The private sector can bring in efficiency to distribution channel as also leverage capital efficiency. Accordingly, policy should be designed to now decontrol the sector," Mahurkar suggested.

Whatever the glitches going forward, PMUY is one scheme for which this government can unambiguously claim credit as a controversy-ridden poll season begins.

INSIGHT

The importance of central bank communication

The RBI should think of providing signals that reduce the disconnect with market expectations

SOUMYA KANTI GHOSH

Central Bank communication across the world has been the subject of much intellectual discourse, but it has almost always been in the context of the communication of monetary policy. That is understandable because monetary policy is at the heart of central banking and also because communication of monetary policy is possibly more challenging than communicating other policies.

Over the last two decades, central banks have moved towards clearer communication and greater transparency. This has been driven by several motivations. First, central banks have realised that open and transparent communication enhances policy effectiveness. This shift reflects a shift in the theory of monetary policy. Until the early 1990s, monetary policy was strongly influenced by Robert Lucas' argument that monetary policy affected real variables only if the policy changes were unanticipated. This encouraged obscurity over openness and clarity. Lost in the message was the fact that monetary policy always affected nominal variables like inflation even if fully anticipated. In the 1980s, Finn Kydland and Ed Prescott argued that fully transparent rules rather than discretionary policy changes were more efficient and credible. This was the beginning of the push towards rules over discretion and greater central bank transparency.

The most eloquent illustration of this shift is the change in the communication strategy of the US Fed. Prior to 1994, the US Fed didn't even announce the target Fed Funds Rate (FFR); the market was expected to infer the rate from the timing, sequencing and magnitude of its open market operations. In contrast, today, the Fed not only announces the rate but also gives a clear indication of future policy trajectory. Indeed, it is standard practice for central banks these days to indicate the policy rates, the rationale behind the policy action, the expected outcomes, and often, forward guidance on future policy actions.

Central banks have embraced more open communication to counter the criticism that an autonomous central bank comprising unelected decision makers was inconsistent with a democratic structure

While communicating policy after it is made is the standard mode of communication, central banks are taking to communication before policy action. This again is a lesson from experience — that the market does not like unexpected news, and that surprises should be avoided unless surprise is, in rare circumstances, part of the strategy itself. When the Fed announced it would reinvest the proceeds of maturing securities purchased under the first phase of quantitative easing (QE1), the markets were unnerved. In contrast, the elaborate communication exercise that preceded the QE2 delivered the expected announcement effect. QE2 has of course come in for extensive criticism, but that is certainly not because of lack of communication.

The Reserve Bank of India (RBI) had a similar experience. Both on the way up to the crisis and on the way down, it had to make several off-cycle policy adjustments. There was wide agreement that these measures were expedient but they did not go down well with the market because of the surprise element. This prompted the RBI to revise its communication strategy by introducing, with effect from September 2010, more structured mid-quarter reviews (now bi-monthly). Such frequent policy reviews reduced the need for off-cycle action, minimising the surprise element. In recent times, the RBI has been putting in a subtle message of policy changes through its monthly and annual publications, that sometime escapes attention.

Sometimes communication, instead of being a vehicle for policy, can be the policy itself. Drawing yet again from the US experience during the crisis, the Fed realised that its repeated announcement/first generation policy signals of keeping rates low "for an extended period" or "can be removed at a pace that is likely to be measured", led markets to reach a certain inference on what the "extended period" could mean. The ECB's use of such code words as "strong vigilance" also belongs to this category.

Some policy analysts argued that a step that the Fed could consider was to modify the language of the statement (second generation signals as Bank of Canada does) to provide exact information to the markets. This, it was believed, would ease financial conditions as desired. In August 2011, the Fed enhanced its guidance, which until then had stated that the FFR would likely stay at exceptionally low levels "for an extended period", by replacing the latter with "at least through mid-2013". Simultaneously, to make its objectives clearer, in January 2012, the FOMC (Federal Open Market Committee) released a Statement on Longer-Run Goals and Monetary Policy Strategy.

In the Indian context, the RBI typically provides first generation signals in its policy statement. We believe the RBI should think of providing signals that reduce the disconnect with market expectations.

Another factor that has motivated central banks to place a bigger emphasis on communication is their hard-earned autonomy in the years before the crisis. Central banks have increasingly embraced more open communication to counter the criticism that an autonomous central bank comprising unelected decision makers was inconsistent with a democratic structure.

Before we conclude, here are two things to remember. First central bank communication is important for the institution to learn, listen and understand. One is referring here not to the standard one-way oral or written communication but to two-way communication between the central bank and its stakeholders, with the central bank remaining largely on a listening mode as the RBI does at periodic intervals. Second, continuous interaction with market (social media included) and all stakeholders is the best strategy for policy effectiveness and helps deflect threats to central bank credibility.

The author is group chief economic advisor, State Bank of India. Views are personal

LETTERS

No compromises please

Media has reported that the Centre has rejected 11 names for appointment to the high courts and the collegium of Supreme Court judges has accepted the decision. In the first place there are a few questions to be answered, which the media must ask: How were these names even proposed? Can these names be considered and even appointed later if the personalities in the Centre and the collegium change? What posts are these 11 people holding? Are they holding judicial appointments in lower courts? If they are tainted, how can they even hold these posts? Is there a graded scale of "adverse material" for appointments at various levels in the judiciary?

These 11 names must be made public so they are not considered and even appointed in future. In fact, if they are tainted, they should be removed. There cannot be arrangements and compromises between the parties concerned, at least, not in the interest of the country.

T R Ramaswami Mumbai

Some missing points

This refers to "Soon no e-way bill if GST returns not filed for 6 months" (January 21). The report says non-filers of Goods and Service Tax (GST) returns for six consecutive months will soon be barred from generating e-way bills for movement of goods. This is true for composition schemes. Regular suppliers have to file monthly returns and the e-way bill generation will be barred if GST returns of two consecutive months are not filed. Another important fact that has been missed out is that this provision will come into play if either the buyer or the seller has not filed returns for two consecutive months. This would result in defaulting suppliers also losing business as in that case, the buyer will be forced to deal with another supplier.

Rajeev Khandelwal via email

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HAMBONE

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Focus on the primary

Multiple responsibilities should not detract

In a speech last week, Reserve Bank of India (RBI) Governor Shaktikanta Das stoked an old debate. He referred to one of his tweets in October 2018 that said "Central banks across countries have a very critical role at the current juncture. The challenge is to try and read the situation and take decisive steps in pursuit of their multiple responsibilities." Mr Das said as the RBI governor, he would now act according to these principles. His comments were significant because two of his immediate predecessors, Raghuram Rajan and Urjit Patel, wanted the RBI to "exclusively focus" on inflation targeting. In fact, in November 2016, the RBI Act was amended to redefine its goal as "maintaining price stability keeping in mind the objective of growth." Thus, the emphasis on "multiple responsibilities" by Mr Das has been seen as a significant shift in the RBI's approach.

The fact is that the RBI, via the monetary policy committee, which has an equal number of nominees from the Union government, is required to maintain retail inflation, as measured by year-on-year changes in consumer price index, at the 4 per cent mark. However, the RBI has been given a leeway of 2 percentage points on either side of this central mark. This essentially means that there is enough possibility within the 4 percentage point band — between 2 per cent and 6 per cent retail inflation — for the RBI to focus on other concerns such as growth. It is possible to argue now that India has reasonably low inflation. After all, as the RBI Governor noted, India has witnessed significant disinflation since 2012-13, with headline CPI inflation moderating from an annual average of 10 per cent in 2012-13 to 3.7 per cent in 2018-19 so far (April-December).

Indeed, headline inflation was just 2.2 per cent in December 2018. Yet, while lower inflation should allow the RBI to focus more on growth, the fact is that India still has some worries on the inflation front. For instance, non-food, non-fuel inflation has been high (close to 6 per cent) and persistent. There are also concerns about financial stability, especially at a time when there is much churn in the non-banking financial sector. As such, it would be best that the RBI stays vigilant and does not let its guard down on its primary responsibility.

In fact, in the context of overall macroeconomic stability of the system, there are growing concerns on the fiscal policy front as well. Thanks to a flurry of policy choices — such as blanket farm loan waivers, higher minimum support prices, etc — it looks increasingly tough for governments, both at the Centre and the states, to meet their fiscal deficit targets. Indeed, with slippages on the revenue front as well as likely sops in the Budget, such as direct income support, it is quite likely that India will struggle to meet its public debt-to-GDP ratio target of 60 per cent. The trouble is, once put in place, it is politically difficult to overturn these policy choices, thus lending permanence to these expenditures. The RBI as well as the central government should not allow their "multiple responsibilities" to come in the way of their legally mandated commitment on inflation and fiscal deficit target, respectively.

Data protectionism

India's data belongs to its people, not to Indian companies

Speaking at the Vibrant Gujarat summit in Ahmedabad, the chairman of Reliance Industries Limited, Mukesh Ambani, drew attention to questions about the ownership of personal data that will be an important subject for regulators going forward. Mr Ambani argued that "data is the new oil in the new world order" and that "data is the new wealth". Therefore, "India's data must be controlled and owned by Indian people — and not by corporations, especially global corporations". Mr Ambani is correct on the assumptions embedded here, and he needs to be congratulated for repeatedly raising the issue of data ownership as central to the future growth trajectory of India. However, there are also questions that are raised by Mr Ambani's formulation, especially in the context of recent regulatory and policy moves in India.

Mr Ambani — who also controls Jio, which has disrupted the telecommunications and data sector in India — is not wrong when he says that "India's data must be controlled and owned by India's people" rather than by corporations. However, it might be seen as somewhat self-serving for him to draw a line between global and Indian corporations in terms of policy here. That cannot and should not be seen as a basis for the drawing up of consumer-focused policy on data ownership. Once data ownership rights are assigned to individual Indians, it should be left up to them how they further dispose of what is, after all, their property. If they get a better "price" or services from a non-Indian company, then they should be able to re-assign rights to them, subject to certain national security limitations. This is, after all, a basic free trade principle applied to this domain. It will, as in other domains, ensure that consumers get the highest possible utility while ensuring that competitive forces are given full play. The alternative would be to create a group of privileged Indian corporations that are insulated from competition, and thus can take advantage of consumers. This digital 'Bombay Club' argument cannot be allowed to stand.

The context of this discussion is important to note. Several recent flash points to do with data localisation have emerged between companies and regulators. The Reserve Bank of India last year ordered payments systems to store all their data locally for "better monitoring" by the RBI. This was a poorly considered move, as it would increase the cost of payments architecture— and, incidentally, reduce privacy of Indian citizens. Worse, a government-appointed committee has demanded that not just payments, but all data centres for companies serving Indian citizens be located within the physical borders of India; a similar rule might be applied to e-commerce companies. All of this erects unacceptable barriers to trade and harms consumers in the name of protecting Indian data. Indian consumers should be the focus of such regulation, not Indian companies or Indian bureaucrats. The government and regulators should thus consider the principles that Mr Ambani upholds, but not implement them in such a way that only Indian companies benefit.

ILLUSTRATION BY AJAY MOHANTY

Restoring rural cash flows

Low food prices hurt cash availability in the rural economy, and loan waivers make that worse

"*Bazaar mein paisa nahin hai*" (there is no liquidity in the market) has become a common refrain of distributors and wholesalers and, in particular, is heard in any discussion on agricultural markets. It is a phrase that makes little sense at first. Sales should just be driven by demand and supply after all; what does money have to do with it? But you need money to facilitate transactions, and the informal economy, which accounts for more than 40 per cent of the country's GDP, only runs on cash — that is, physical currency. That nearly all of agriculture is informal makes it one of the most cash dependent sectors. In theory, the same amount of cash can support more economic activity if the velocity goes up (that is, the number of times a currency note is used in a year), but this does not change quickly, and to grow the informal economy by, say 10 per cent, the cash available should also rise by broadly the same amount.

TESSELLATUM
NEELKANTH MISHRA

What has driven this tightness in cash? Some observers have linked this to demonetisation; that despite the currency in circulation being nearly 14 per cent higher than what it was pre-demonetisation, the re-monetisation has not been smooth and there are pockets that still do not have enough cash. It is hard to do rigorous analysis given the paucity of granular data, but it appears that there may be other reasons.

Cash starts its life in the formal economy: The central bank prints it and gives it to the banks. Once withdrawn from banks, it is hard to track its movement (at least for those not working for regulators), but one can think of some large pathways through which cash moves into the informal economy. The first is food procurement: Non-agricultural workers (the net consumers) purchase upwards of ₹15 trillion from farmers (net producers) annually. Then, there are farm loans. After the farmer gets the loan amount in his account, he withdraws the cash to make the necessary payments for inputs like labour, seeds and fertilisers. Land purchases also transfer potentially large sums of money to the cash economy.

In the last few years, each of these pathways has narrowed. Weak prices for farm products over four years have not only slowed the transfer of income from the mostly better off net consumers to the mostly poor farmers, they have also likely hurt the availability of currency in the farm economy. Loans have stagnated too. Five years ago, the net annual increase in agricultural loans used to be well over a trillion rupees; this number today is lower even in absolute terms. Similarly, with green-field project announcements mostly absent and stress in the real-estate market, land acquisition activity has been weak too.

Mismanaged farm loan waivers make this problem worse. Governments announce waivers in a hurry but then take years to execute them. The loan burden on the farmer eases for sure, but the benefit in terms of net cash availability is only the interest that was due (7 per cent annually on most of these loans). What makes things worse is that during the unduly long period of execution, banks are reluctant to issue new loans in these areas. The flow of funds to these areas thus slows, and, in fact, hurts the economy.

A farmer support scheme though may be hard to avoid. As an economy develops, one inevitably reaches a point at which the per capita income from farming falls behind non-farming income. Other than in countries such as Australia and New Zealand, with large per capita land availability, agricultural income would struggle to compete with that in manufacturing or services. Therefore, subsidies to agriculture are common. Swiss agricultural subsidies, for example, are more than 80 per cent of Swiss agricultural output— that is how one of the richest countries in the world can afford to keep cows.

If it can be executed well, a direct income transfer scheme may be a better option to help farmers, as it gets cash flowing into this part of the economy. In the socio-economic caste census — it was used recently for the health insurance scheme and also quite successfully for the rural housing subsidy — the government has a tool to direct the transfers to the needy that was not available till a few years ago.

There is some fiscal space too, though not a lot. Beneath the apparent stagnation in fiscal consolidation over the past few years, there has been some under-appreciated improvement. Every 10 years, the ratio of government salaries and pensions to the country's GDP rises sharply, and then falls till the next pay commission raises it again. In the fifth pay commission (1997-1999) the increase was about 2 per cent of GDP and in the sixth (2009-11) it was nearly 2.5 per cent. During the seventh pay commission (2017-19) the increase has been only about 1 per cent, and the aggregate fiscal deficit has not changed, unlike in prior decades. Going forward, as the growth in government salaries and pensions normalises (at least till 2027, when the next hike is due), the ratio may drop by 0.3 per cent next year, and 1.1 per cent by 2023. Next year, this creates more than ₹60,000 crore of fiscal space between the Centre and the states.

If one assumes that the bottom 30 per cent of the rural population will be targeted, the second order effects may also be helpful: 60 per cent of the consumption basket in this segment is food. Demand for more expensive calories —such as milk, oil, meat and eggs — could pick up, providing some boost to prices of these primarily agricultural commodities and thus improve the transfer of income and cash to the net producers.

These are, however, assumptions and the economy could react very differently too. A transfer scheme at this scale is untested and the potential impact on the economy is hard to assess. Necessary as it is, this is also not a cure to the problem of low farm incomes but only provides symptomatic relief. Unlike in the more prosperous economies that have farm subsidies, a very large part of India's workforce is in agriculture. Finding them alternative employment as well as boosting farm exports are the only sustainable solutions.

The writer is co-head of Asia Pacific strategy for Credit Suisse

Missing the wood for the trees

Several commentators and economists have expressed concerns about the arithmetic underlying the government's fiscal deficit calculations, spurred by a recent report by the Comptroller and Auditor General (CAG).

The report points out that (1) government has not reimbursed the Food Corporation of India and fertiliser companies fully for food and fertiliser subsidies (while paying interest on loans to finance these dues). (2) NABARD funds an irrigation programme that is a central government scheme that was previously funded through the budget.

The report says that these expenditures in 2016-17 "were through off-budget financing route with fiscal implication of understating government's expenditure in the year as they were deferred" (sic)

RATHIN ROY

The information provided is accurate but the conclusion misplaced. The fiscal deficit of the central government is simply the difference between its revenues and expenditure. If an agency of government incurs expenditures that were previously incurred within the budget then that's an executive choice. It is not an understatement of the fiscal deficit, just as if a private conglomerate finances an expenditure through one of its own companies instead of through the income of the holding company, this would not be seen to be "understating the expenditure of the holding company".

This may (or may not) have implications for the overall health of the conglomerate, but there is no violation or concealment involved. If government uses taxes to write-off Air India's losses, then it would be ridiculous to say that Air India is understating its losses. The CAG report incorrectly uses the phrase "understating government's expenditure," leading to uninformed confusion.

The report also charges government with deferring current year liabilities to the next year. While this is true, it is not illegal. No conclusion about deficits in future years can be drawn. Government may in future years continue to defer liabilities or pay them off by raising taxes and/or reducing expenditures, thereby sticking to its fiscal deficit commitment. No ex ante judgment can be drawn on this score. An auditor's dislike of unpaid bills and rollovers does not implicate the rectitude of government's fiscal reporting.

Some commentators say that such borrowings add to the public sector borrowing requirement (PSBR). This is not true. The PSBR is the sum of borrowings by government and all public sector entities. The location of the borrowing does not impact the PSBR. If someone thinks government borrowing equals the PSBR then this is an analytical error and not a consequence of fiscal jugglery.

This misplaced excitement at having uncovered some non-existent fiscal jugglery is a consequence of lazy analytical thinking which governments cheerfully exploit. The things the CAG report interdicts have been bipartisan practice. Governments of all hues have escaped scrutiny of the overall debt of the public sector because there is no pressure to install the analytical equipment that would support such scrutiny. Ideally, there should be a PSBR calculation undertaken and placed in the public domain. NIPFP has tried to do this and while we have come up with credible estimates, there is a formidable analytical challenge in India. A large chunk of the financial system and corporate sector is publicly owned. So should lending by public sector bank to a public sector corporation count as an increase in the PSBR? And what of acquisitions of public entities by other public entities? There are answers to these questions, but these are open to challenge as there can be ambiguity in interpretation. Within these limitations, it is reasonable to conclude that the non-government public sector borrows around 1.2 per cent of GDP; this is a fairly constant number in recent times. An important driver of the case of fiscal consolidation made in both the FRBM reports is that this means that the combined borrowing of central and state governments and public sector entities is more than 8 per cent of GDP. With financial savings around 11 per cent, this makes capital scarce and expensive for the private corporate sector. This practical fact is ignored by both proponents and opponents of fiscal responsibility. They prefer the easy and lazy route of casual questioning of government motivations, missing the wood for the trees.

They also ignore the hard and unglamorous task that is key to fiscal reform in India. A medium term fiscal framework with intertemporal fiscal projections would clearly reveal the medium term implications of both single and multi-year government fiscal decisions and facilitate calculation of a credible PSBR. In such a framework, the multi-year implications of a specific fiscal action would be apparent and government would be accountable for these.

I have ploughed a lonely furrow pleading with analysts to support the case for government to shift to such a framework, the basis for fiscal strategy and management in most modern economies. Analysts pay lip service to the idea but continue to focus on annual budgets (and, even more silly, on intra-year budget numbers). It is time to get serious about this major structural weakness and collectively persuade government to upgrade its annual budgeting process to a 3-5 year operational fiscal framework. Only this will improve the quality of fiscal execution and transparency.

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The spectre of BJP

BOOK REVIEW
BIBEK DEBROY

Sagarika Ghose's book is described as "A manifesto for Indians who believe in individual freedom". Apart from a longish introduction, there are five chapters — Liberal Patriot, Liberal Hindu, Liberal Thinker, Liberal Dissenter and Liberal Woman. Each chapter has a sub-title that reveals what this book is about. Respectively, these sub-titles are: Why the liberal Indian is a greater patriot than the 'Hindutva nationalist'; Why the true Hindu is always a liberal and why the liberal Hindu is a better Hindu than the political Hindu; Why the liberal who believes in enhancing the power of the individual is a better democrat than the liberal who believes in increasing the power of the government or the state; Why the liberal dissenter is not a traitor and why free-thinking intellectuals are crucial for a nation's progress; and Why the liberal must always oppose those who discriminate against and stereotype women, crush their freedoms and force them to be caricatures of an imagined 'Indian culture'. As these sub-titles reveal, and as the pages elucidate, from the author's perspective, the spectre haunting liberal India is the Narendra Modi government and the Bharatiya Janata Party, though she makes both sound like the James Bond SPECTRE. Wearing biases on the sleeve is good for transparency, though.

We should start with some definition of liberalism. "There is little agreement on what liberalism exactly means, although all liberals are united in their primary belief in limited government, autonomous institutions, individual freedom and the rule of law...It took three years of debates in the Constituent Assembly, each Article tortuously debated, for us Indians to gain our liberal, individual-rights-centred Constitution."

That 1950 Constitution has been amended several times. With such admiration for that individual-rights-centred Constitution, I would have expected some discussion, if not of all amendments, at least the First Amendment, especially because it was about "abuse of freedom of speech and expression", consequent to the 1950 case, *Romesh Thapar* versus *State of Madras*. Indeed, a liberal should object to all aspects of First Amendment — Article 19(1)(a), 19(1)(g), 19(6) and 31. The only reference I could find to First Amendment was the following: "Interestingly, Shyama Prasad Mukherjee, Vajpayee's precursor in the Hindutva nationalist movement and the founder of the Jana Sangh, can be called a liberal in some respects as he had argued strongly against Nehru's first amendment of the Constitution, which restricted freedom of speech." So, Syama Prasad Mukherjee can be called "a liberal in some respects". There is no such hesitation about Jawaharlal Nehru or B R Ambedkar. "India's first prime minister, Jawaharlal Nehru, differed with Gandhi on the role of the government. Yet, he was a quintessential social liberal and constitutional democrat," Ghose writes. And "B R Ambedkar, draftsman of the Constitution, was also a quintessential liberal."

Not only did Syama Prasad Mukherjee oppose the First Amendment, both Nehru and Ambedkar supported it. Interestingly, Ghose doesn't mention this, perhaps because that would have invalidated the simplified spectre proposition. (The spelling should be Syama Prasad, not Shyama Prasad. I don't understand why she got that wrong, just as I don't understand why she got a few minor words in Tagore's "*Hey more chitto*" wrong.)

Though Ghose pegs the book to the present government, blamed for an increase in illiberalism, let's focus on that core liberal agenda, as defined in the book —limited government, autonomous institutions, individual freedom and rule of law. She says, "In an earlier time, a socialist-based ruling party under Indira Gandhi had launched an all-out drive for making India more socialist with campaigns like the 20 Point Programme." The 20 Point Programme was initially launched in 1975 and has been restructured thrice since then. Per se, it is difficult to see how the original 20 Point Programme incorporated socialism, as opposed to other policies that drove the agenda. Be that as it may, as a liberal, I ought to object to Section 29A(5) of the Representation of the People Act (1951) that requires all political parties registered in India to be socialist and to the 1988 amendment that introduced this clause. I ought to object to the 1976 amendment to the Preamble, making India socialist. "The public-sector-guided economy was the dominant belief in Nehru's time," she writes. As a liberal, I ought to applaud B R Shenoy's minute of dissent in 1955 and condemn his subsequent ostracisation, symbolic of a threat to autonomous institutions.

"Rule of law" is a handy expression, but it is conditional on the law and no legislation is ideology-neutral. Any statute is a curb on individual freedom, more so since statutes can be coloured by ideology. Imports of Alexander Campbell's 1958 book, *The Heart of India* were banned in 1959. As a liberal, do I support the ban? As a liberal, do I support the relevant section of the Customs Act that enables government to impose such a ban? There can be an intrinsic incompatibility between a liberal position and the rule of law. Any liberal manifesto should discuss such issues. But this book doesn't. Nor are the instances I have cited (Representation of the People Act, Preamble, Shenoy, import bans) mentioned. That's because this well-written book's implicit title is, "Why I am against this government".

WHY I AM A LIBERAL
A Manifesto for Indians Who Believe in Individual Freedom
Sagarika Ghose
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