Winners and losers

What does the withdrawal of USGSP benefits mean for India's exports?

ANWARUL HODA & NEHA GUPTA

On March 5, 2019, the United States Trade Representative (USTR) announced the US government's intention to terminate the benefit of duty-free treatment under the generalised system of preferences (GSP) for products imported from India. How much of a setback does this constitute for India's exports?

Within 60 days of the notification, imports from India of products now included in the USGSP scheme will be required to pay MFN duties. The preliminary assessment in India of the damage to the country's trade interest has been dismissive.

There are a number of reasons for the apparent lack of concern in India at the USTR decision. From the outset, the USGSP scheme was designed to result in diminished benefits for countries like India, which export labour-intensive products. The US law mandatorily excludes most textile and apparel articles, footwear, handbags, luggage, flat goods, work gloves, and leather apparel from the purview of the scheme. Further, a central feature of the USGSP scheme is the competitive need limitations, which imply that individual beneficiary countries are excluded once imports from any one of them cross the stipulated value limit, or if they exceed a 50 per cent share of imports from all beneficiaries in a particular year. There is provision for the restoration of benefits if in a subsequent year imports from that country fall below the prescribed limits. However, the re-designation of a country as a beneficiary is not automatic. The switch on or switch off of benefits by virtue of the competitive need limitations reduces the value of preferential benefit in promoting industrialisation of developing countries, which was the main aim of the programme.

Another reason for the reduced value of the USGSP is that the US has granted more comprehensive benefits to nations that have entered into FTA agreements with it. NAFTA and KORUS FTA agreement, for instance, give duty free treatment to Mexico and South Korea respectively far greater in scope than is available to GSP beneficiaries. An even more important reason is the erosion of tariff benefits under the GSP due to the reduction of US MFN tariff in successive rounds of multilateral trade negotiations. The USGSP scheme was introduced on January 1, 1976, and since then, the US has reduced the MFN tariffs twice, in the Tokyo Round concluded in 1979 and in the Uruguay Round, which ended in 1994. In 2017, the MFN tariff applied level in the USA was 3.4 per cent and the trade-weighted average 2.4 per cent.

But averages conceal great divergences and to make a proper assessment of the impact, we need to look at the tariff situation on each product. US MFN tariffs are significant on many products and the effect of GSP withdrawal will depend on the level of MFN duty that will apply once the GSP treatment is withdrawn.

Our assessment is that about US$3.3 billion worth of Indian exports to the US, on which the MFN duty is more than 2.5 per cent, will be adversely affected. Of this, the export of products amounting to about $1.4 billion on which the MFN duty is higher than 4 per cent is likely to be particularly affected. The most important group of products that will stand to lose is chemical and allied products, valued at about US$ 519 million, on which tariffs will apply in the range of 4-6.5 per cent. Iron and steel products, including some categories of hand tools, valued at $177 million will be hit by duties in the 5-15 per cent range.

Another segment of industry that will suffer from tariff increases in the range of 4-20 per cent is travel goods (mostly non-leather), including suitcases, handbags and sports bags, in which imports from India are at $253 million. An equally important section of industry that will be hit with tariffs of 4-20 per cent is handicrafts (lamps, parts, chandeliers etc), in which the current level of US imports is about $109 million.

On the whole, the negative fallout of the US decision to withdraw GSP benefits from India is assessed at modest but not trivial. But the effect on certain sensitive sections of small and micro industries should be a cause for concern.

Should the government have done something to stave off action by the US government? Even though the GSP benefits are required to be non-reciprocal according to the UNCTAD resolution in which it was agreed and the GATT 1947 decision that incorporated preferential treatment of developing countries in the rules, US laws have provided for seeking reciprocity from beneficiary countries from the beginning and these laws have not been challenged. According to reports, negotiations did take place between the two sides in the two areas of US concern on which it sought concessions, namely, market access in dairy products and regulations governing medical devices, but success proved elusive.

Hoda is professor & Gupta is fellow, ICRIER

A knowledge gap at CCI

The competition regulator is ill-equipped to handle the intricacies of digital markets

SUBHOMOY BHATTACHARJEE

A *Reuters* report a few weeks ago noted that the Competition Commission of India (CCI) is probing whether Google's Android mobile operating system has been used to block its rivals. As the fair market regulator, the CCI should be examining such issues. But it appears to be venturing into areas where it has not shown any strong degree of perspicacity.

Digital markets are new territory for all competition regulators worldwide. At one level, markets are intuitively easy to understand. They are a place (physical, spatial, neural) where goods, services and now data are bought and sold. An enterprise can be seen as anti-competitive if it aims to reduce competition and maintain levels of profit. Yet, unless carefully drawn, identifying the relevant antitrust market could be tricky in the digital space since a non-market could also end up seeing like a market.

TAKE TWO

Why shouldn't the CCI be able to navigate this terrain? The principal reason is that the regulator has not concentrated on building up its internal capacity since its formation in 2009. It has traditionally packed its bench with retired or about-to-retire bureaucrats who have held numerous impressive posts earlier but have shown no specialised knowledge of the domain of the anti-competitive body. Or they have been lawyers or judges. But CCI, despite its powers to impose penalties, should not be seen as a court. The present composition of three members includes only one economist, selected after a long gap. There has been nobody from finance or from any technology sector. In the absence of specialists, CCI has examined competition issues on the basis of legalese rather than as economic issues.

One can draw on two examples. In 2018, CCI published a competition assessment toolkit to guide ministries and the world at large on what constitutes fair competition. The slim volume has no mention of digital economy in a world where the top four global brands belong to this category. Instead, it perceives competition as essentially freedom from government policies and laws that circumscribe markets. Competition assessment involves "identification of relevant legislations and regulations; application of checklist to be applied to the selected legislations/regulations to find out provisions having competition concerns; finding alternatives to those provisions in consultation with concerned stakeholders, choosing the best alternative for modification; and carrying out post modification impact assessment". These are important for an economy like India but fall short of the demands of a digital economy.

The second example is the case again involving Google filed jointly by matrimony.com — a network of matchmaking services, whose flagship brand is Bharat Matrimony — and advocacy group CUTS. This was CCI's first intervention in the digital space.

In February last year, the Commission by a 4 to 2 verdict held that Google India had run foul of competitive behaviour in what is known as the "intermediary services market" and fined it ₹136 crore. The problem is in the way the regulator agreed to splitting the online market, as the dissent notes too pointed out.

In the digital space, companies such as Google or a taxi service aggregator offer what is called multi-sided business platform. They bunch up those demanding a ride on one side and those offering a ride on a separate platforms. Those platforms create economies of scale but do not create a market by themselves. The market comes into existence only when those demanding a ride and those offering one come together. Entities like Google use their ability to create innovative business models to attract more people from the two sides to board the platforms. Yet, the regulator defined those platforms as markets by themselves and then went on to determine if the company is a dominant one.

In the matrimony case, the CCI held that Google created a search bias on these platforms. While the Commission did not link its order to adduce any matrimony-related case, it offered the example of what happens when consumers book a flight on the web. Instead of taking consumers directly to portals that offer specialised services for flight bookings, Google prominently places its own flight listing on the search page which "is able to drive traffic to its own (commercial) pages and also generate revenues through advertisements/sponsor results". Since web services depend on user-traffic such an "unfair diversion of traffic by Google may not allow third-party travel verticals to acquire sufficient volume of business... Thus, the CCI held that Google was leveraging its dominant position in the General Web Search to promote its Commercial Flight Units".

What the CCI failed to see was that the digital markets are a great arena for the spread of what is called network economics. Shorn of jargon, it is the ability of firms in these spaces to connect consumers on platforms. Naturally, for network economics to flourish, it needs depth in the market. Two things become important in this context. Network economics disproportionately encourages companies to expand. But to expand, companies need to innovate, which often comes through price changes. A Flipkart, Snapdeal and Amazon emerge because of this advantage.

Would this impact the Google Android case? Here, too, it is a case of network economics. But as the European Commission has already fined Google €4.34 billion for allegedly using Android mobile devices to strengthen the dominance of its search engine, it remains to be seen if the Indian regulator is able to draw its own conclusion independently. The matrimony case was filed with CCI in 2012 but took about six years to be discharged. Did the regulator wait? Meanwhile the EU, on a similar case related to Google Shopping, issued a statement of complaints in 2016 upholding the charges of discrimination against the internet search company.

CCI needs to create regulatory muscle to wrestle with the arguments either way. This does not mean that the regulator needs to slip back into a larger body as it was till last year. It must instead demonstrate it has the wherewithal to handle such cases without simplifications that often get scuttled at the next appellate stage.

CHINESE WHISPERS

More sons & daughters

The Dravida Munnetra Kazhagam (DMK), the main rival of the ruling All India Anna Dravida Munnetra Kazhagam (AIADMK) in Tamil Nadu, has released the list of its candidates for the Lok Sabha election. Of the 20 names, seven are party veterans and 13 are new faces, including daughters, sons and relatives of DMK leaders. The first family of the DMK was represented by Kanimozhi, daughter of the late M Karunanidhi and sister of DMK President M K Stalin (*pictured*), and Dayanidhi Maran, a cousin of Stalin. The list also included names like T M Kathir Anandh (for the Vellore seat), son of DMK Treasurer Duraimurugan; former state electricity minister Arcot N Veerasami's son, Kalanidhi Veerasami (Chennai North); and Dhanush M Kumar, son of former AIADMK MLA Dhanuskodi, who joined the DMK (Tenkasi reserved). DMK leader Ko. Si. Mani's very close aide S Ramalingam will contest from Mayiladuthurai. P Velusami, who contests the Dindigul seat, comes from a family deemed close to the DMK.

Theft at Vaghela's residence

Cash and jewellery worth ₹5 lakh were stolen from former Gujarat chief minister Shankersinh Vaghela's house near Ahmedabad, allegedly by a domestic help couple from Nepal, the police said on Monday. The theft at the residence of Vaghela, a former Congress leader who is now in the Nationalist Congress Party, took place in October last year, but a police complaint was lodged only Sunday by Vaghela's employee Suryasinh Chavda, they said. According to Chavda's complaint, the suspicion fell on the husband-wife duo after they did not return from Nepal as promised, the police said. As the media reported the news, the Twitter hashtag "*chowkidar chor hai*", an apparent dig at the Bharatiya Janata Party's *Main Bhi Chowkidar* campaign, also started trending.

Dealing with trust deficit

The Congress party in Haryana is at war with itself. Such is the trust deficit in the state leadership that the party's state leaders like former chief minister Bhupinder Singh Hooda, Kumari Selja, state unit chief Ashok Tanwar, Kuldeep Bishnoi and others do not see eye to eye. On Friday, they forced Ghulam Nabi Azad, who is in charge of the party's Haryana affairs, to withdraw a list of 15-member coordination committee for the Lok Sabha polls. Azad said he was planning to replicate an experiment he successfully conducted in Andhra Pradesh and Karnataka when infighting had plagued the party units in these states in the early 2000s. Azad said that in Karnataka in 1999-2000 and undivided Andhra Pradesh in 2003-04, he hired a bus and put all the Congress leaders in it to travel across the states. "They would eat at the same place, address public meetings from the same stage and spend time with each other during travel, which built trust. I need to do something similar in Haryana," Azad said.

ON THE JOB

Tragedies of the educated unemployed

MAHESH VYAS

The unemployment rate among those who had completed graduation or higher education (graduate+) has been rising steadily since mid-2017. During September-December 2018, the unemployment rate among these had reached 13.2 per cent. A year ago, the unemployment rate in this group was 12.1 per cent.

Graduate+ face the highest unemployment rate among groups of individuals organised by the level of education achieved. It is usually twice the average unemployment rate for the entire labour force. It is worse for graduate+ women.

We consider five groups of individuals by the maximum level of education they obtained — those with no education; those with education up to fifth standard; those with education between sixth and ninth standard; those who cleared tenth, eleventh or twelfth standards; and those who completed graduation or any higher level education than graduation.

During September-December 2018, the average unemployment rate was 6.7 per cent. The uneducated did not face much unemployment as the unemployment rate for them was a negligible 0.8 per cent. These are likely to be the poorer people for whom unemployment is not a choice. They have to take up any job, no matter how poorly paid or however risky. The next group, those with education only up to fifth standard, also faced a very small unemployment rate of only 1.3 per cent. The compulsions to take up a job for this group could be no different from the earlier one.

The unemployment rate rises to 4.6 per cent for those who had completed between sixth and ninth standard. For those with qualifications between tenth and twelfth standard, the unemployment rate was uncomfortably high at 10.6 per cent. Then, it rises even higher to 13.2 per cent for graduate+.

This rise of the unemployment rate with rising education levels indicates that India is unable to produce sufficient decent quality jobs for the better educated. And, the better educated are not willing to take up just any crappy job.

The graduate+ section of society is the one that is the most qualified to be employed. But, the higher unemployment rate of these people shows that India does not produce sufficient decent jobs for its graduates. This is the tragedy of India's employment problem — its higher unemployment for the better educated.

A person with less education has a lesser degree of freedom and so is often compelled to take the available low-paying, low-quality jobs or more often undertake extremely low-quality self-employment. This keeps the unemployment rate in these groups low. But, self-employment is more often a compulsion under distress rather than a choice over a safe job. This is the greater tragedy of India's employment problem.

CMIE's Consumer Pyramids Household Survey shows that graduate+ account for only ten per cent of the working age population of India. This is a rather small proportion.

The stock of graduate+ in India was about 100 million during late 2018. Of this, 53 million were employed. Another 8 million were actively looking for a job but were unable to find one. These are the ones we call the unemployed. The remaining 39 million were not sufficiently interested in working. These 39 million are not considered as unemployed. They are voluntarily not in the labour force and therefore are not considered as unemployed.

India has a very low labour participation rate of around 43 per cent. Education in general, and college education in particular is good for labour participation. Labour participation rates are below 40 per cent for those with education below tenth standard. It improves to 43 per cent for those with tenth to twelfth standard education. Then, for the graduate+ group it shoots up to 61 per cent.

Labour participation rate of graduate+ has also improved from less than 60 per cent a year ago to 61 per cent.

College education makes a big difference to women. Overall female labour participation was extremely low at 11.1 per cent during September-December 2018. But the participation was more than twice as high at 22.6 per cent for graduate+ females.

Over the past one year, female labour participation rate fell from 12.1 per cent to 11.1 per cent. But, labour participation among graduate+ women increased from 21.6 per cent to 22.6 per cent. It was stable at 9 per cent for females with an education level between tenth and twelfth standard. But, it declined for women with lower levels of education.

Graduate+ women face a punishing 35 per cent unemployment rate. This is a tragedy of discrimination. The unemployment rate for graduate+ men was much lower at 10 per cent. Why should the few well-educated women who seek jobs face a much higher unemployment rate compared to men with similar education levels?

The author is the MD & CEO of CMIE

LETTERS

Beyond capital infusion

This refers to "Large fund infusions in PSBs fail to deliver" (March 18). The government has infused ₹1.9 trillion fresh capital into the public sector banks (PSBs) but it has not really improved the share value of most of these banks. First, the investors realise that a fair amount of the funds will be required for fresh provisioning for the stressed assets which will turn into non-performing assets both at the end of financial year (FY) 2018-19 and going forward in FY 2019-20. Second, the financial situations of many PSBs have been shown to have improved by tinkering with the prompt corrective action framework norms. Then, there is the impact of the impending Supreme Court decision regarding the enforceability of the Reserve Bank of India circular of February 12, 2018 on defaulting power companies. Last, the markets realise merely re-capitalising the weak and poorly performing banks without any reforms of either their governance or operational systems will result in a re-play of situation of the last couple of years, in the next few years.

Kicking the can down the road helps postpone uncomfortable decisions but the markets, investors and discerning sections of the public, fortunately factor that in the pricing of the equity of most of the PSBs.

Arun Pasricha New Delhi

A little dirt is good

This refers to "Environment is cleaner, your immune system has never been prepared" (March 17). Experts agree autoimmune disease affects millions of people with a cost of more than $100 billion. Improvements in hygiene and sanitation though welcome have inadvertently given to an alarming increase to human-made auto-immune diseases. It is suspected that this is partly attributable to our lack of exposure to micro-organisms that we once had. Potentially pathogenic and benign micro-organisms associated with dirt once covered all aspects of our earlier lifestyle and ensured an alert immune system. Our immune system needs a level of stimulation early in life to prevent the current rise in autoimmune disease.

Apparently, a little dirt is good for us and our immune system needs this exposure. Like so much of modern life, there seems to be a tipping point when clean is "too clean". Excessive cleanliness is not good and antibacterial agents such as triclosan have been banned in many daily use products such as soaps and toothpastes as they cause more harm and diminish our immunity. A recent development in medicine is faecal transplant for people who suffer from excessive bouts of diarrhoea due to difficult to treat clostridioides difficile infection. A stool transplant from a healthy donor aims to repopulate the patient's gut with good microbes. Another exciting development in medicine is harnessing the immune system to fight cancer. A long-held medical dream is likely to become a reality.

H N Ramakrishna Bengaluru

Empower the forces

India cannot claim to be a power fit to take up a permanent seat in the UN Security Council unless we succeed in making 95 per cent of our armaments. This argument aside, it is perplexing as to why our political leadership has failed to achieve this prime national goal over the last five decades. The answer squarely lies in the gross management ineptitude of our senior bureaucracy who have been allowing precious time to pass by wastefully. There are powerful vested interests embedded in the governments which want to ensure this stalemate continues.

J K Achuthan Ernakulam

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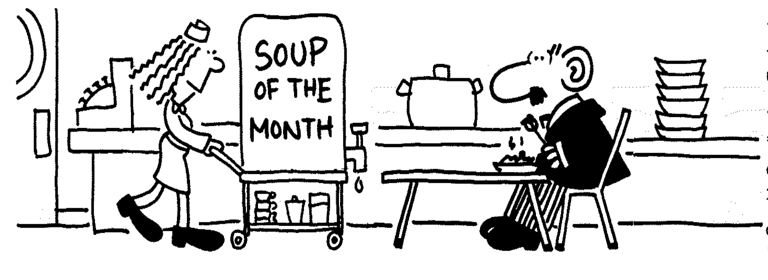
HAMBONE



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Slowdown signals

Next govt faces a daunting economic challenge

India's largest carmaker, Maruti Suzuki, has reportedly cut production by 26.8 per cent in March 2018-19 because of a slowing demand in India's passenger vehicle market. The cutback is significant as it comes after at least three years of strong double-digit growth. Maruti Suzuki isn't alone. A combination of factors, including the tightening of credit norms by financiers and declining urban sales and slowing rural offtake, has forced every other automobile company to pare production. The automobiles sector is just one example of the slowdown, which is gripping the economy. Growth in consumer spending, which accounts for nearly 60 per cent of the economy, had slowed to 8.4 per cent in the October-December quarter, compared with a revised 9.9 per cent increase in the previous quarter, leading policy advisors to worry that the slowdown could hurt the manufacturing sector, hitting engineering, textile and some other labour-intensive sectors. And the worst fears are coming true, as the latest trade data shows non-oil, non-gold imports contracted for yet another month — falling 3.7 per cent in February, following on from a 0.8 per cent fall in January. This is a disquieting trend, as it suggests sluggish industrial demand within India. But the worst may not be over. An expected deceleration in economic growth in major economies around the world, including China and the US, is expected to hurt trade growth further.

That's not all. Industrial growth in January slowed to 1.7 per cent compared to the 2.6 per cent growth in December last year, stoking fears that the fourth quarter of this fiscal year may be as sluggish as the previous quarter. The third-quarter GDP numbers, released by the Central Statistics Office (CSO), showed what most economists were predicting — that growth was slowing. At 6.6 per cent growth, it was the lowest in five quarters. The CSO also reduced its growth estimates for the full year to 7 per cent from the 7.2 per cent estimated earlier. This also means that the last-quarter GDP growth will be even lower. The crisis may accentuate, with weakening global growth (the World Bank has estimated global economic growth to decelerate till 2020 at least), rising oil prices in recent weeks, slowing growth in government spending on infrastructure, and delays in investment decisions because of uncertainty about who will form the next government.

The data from the Centre for Monitoring Indian Economy showed investments in the December quarter fell to a 14-year low, dashing hopes of a quick economic turnaround. The decline in fresh investments was across the board, with all major sectors witnessing a fall. Adding to the gloom is an RBI study that showed that for the seventh successive year, there had been a contraction in the private sector's capital expenditure plans. Other signs of distress are quite high as well. Small and medium industries continue to suffer; core sector growth is at a 19-month low, and third-quarter profit growth among big corporates was at a much slower pace than earlier. Once the elections are over, the new government and its finance minister will have a big problem on their hands — how to fix an economy facing too many headwinds.

The Parrikar vacuum

He provided Goa a liberal, tolerant administration

With the passing of Manohar Parrikar, the Bharatiya Janata Party (BJP) has lost not just a successful chief minister and former defence minister, but also one of its few leaders with the ability and will to bridge the political spectrum and reach out to Goa's minority Catholic and Muslim communities. True, much of this has to do with Parrikar's origins in a multi-ethnic, multi-religious state, where religious polarisation does not win election. Even so, he deserves credit for rising above his Rashtriya Swayamsevak Sangh origins, obtaining a modern scientific education, working as a technology entrepreneur and, later, providing Goa a relatively liberal, tolerant administration during four tenures as chief minister.

Opinion is divided on his effectiveness as defence minister, but Parrikar quickly understood the need to empower the private sector to drive indigenous defence production. His willingness to throw open the door of his office to private industrialists won him a loyal following in the private sector and provided him a valuable reality check on the advice provided by sometimes hidebound administrators who preferred the status quo. He established a "Saturday Club" where he, or his senior officials, met regularly with executives of the private defence industry, leading to a better understanding within the defence ministry of how the private sector was institutionally discriminated against in defence manufacture. Parrikar did more to "level the playing field" than any other defence minister before or after.

Facing a ministerial culture where decisions were often held up owing to the fear of consequences, Parrikar replaced what he openly criticised as a "culture of suspicion" with his own bold decision-making style that cleaved through the Gordian knot of One Rank, One Pension, and other issues that his predecessors preferred to avoid. The ambitious deadlines he set for himself suggested he would have liked to move faster. The reality, however, is he could not. Throughout his 28 months as defence minister, Parrikar remained acutely aware of the importance of retaining a secure political base. Functioning from New Delhi, he remained the de facto chief minister of Goa, flying down on most weekends to set policy and adjudicate disputes within a fractious coalition. His stature across the political spectrum in Goa was underlined after the 2017 elections, when the Congress emerged the largest party, but the BJP persuaded smaller parties and independents to form a coalition around Parrikar. That took him back to Goa, where, despite falling critically ill, he continued functioning as chief minister till the end.

Political turmoil in Goa following his death vindicates Parrikar's belief that he was all that held the BJP-led coalition together. Without a BJP leader who can match his stature, coalition partners like the Maharashtrawadi Gomantak Party and the Goa Forward Party are reconsidering the cost of their support. Leaders of these politically opposed parties have made it clear that they had come together under Parrikar, not the BJP. In its letter to the governor demanding a smooth transition, the Congress has paid Parrikar a backhanded compliment, writing: "Now, after Parrikar's death, BJP has no allies." The BJP, which has been on the lookout for more talent in the government, will surely feel his absence.

ILLUSTRATION: AJAY MOHANTY

How CM Modi predicted PM Modi

If NDA has been resolutely statist instead of leading a market-friendly economic transformation, that should not surprise anybody

POLICY RULES

MIHIR SHARMA

Normally, at this point in a Union government's term — as it approaches the people for another mandate — it would be appropriate to judge it by the numbers. How has it done on growth, given its opportunities? Where would it stand in terms of its various predecessors on this metric? What has been its performance on the deficit, and on focusing on productive spending?

Unfortunately, this is not an option that is easily available in 2019. And the reason is that the numbers that would have to be used for this are, unfortunately, no longer widely trusted. Consider that, according to the GDP numbers — seen together with the back series — India has over the past few years, since demonetisation, equalled or beaten its past economic growth record. This is not generally believed, since the notion that India is growing faster than it ever has is contradicted by most other indicators. Indeed, anyone who lived through the boom of the 2000s will know this is untrue. Last week, over 100 economists from institutions in India and abroad signed a letter complaining about "political interference" in Indian statistics, adding that "any statistics that cast an iota of doubt on the achievement of the government seem to get revised or suppressed on the basis of some questionable methodology".

In some sense, the inability to make comparisons on the basis of state-released data with previous administrations is perhaps the ideal situation for the current government. Few governments in our history were presented with the sort of open goal that the current one was; and there is little doubt that it has, through a combination of poor theory and incompetent management, managed to kick the ball wide.

Many analysts will say that Prime Minister Narendra Modi's performance has been poorer than expected. If anything, that is a consensus. But, in fact, that conclusion is an error of judgment that simply doubles down on the mistakes made by such analysts prior to 2014. The expectation that Mr Modi would be a major reformer, capable of reinvigorating the Indian economy, were based on a complete misreading of both his actions and his performance as Gujarat chief minister.

In 2013, in these columns, I looked at the performance of the "Gujarat model" and concluded that it was based on hype. For example, between 2004 and 2012, growth in per capita consumption in the state had lagged the national average. Under Mr Modi, growth was not increased in Gujarat in that period as much as in, say, the other rich states of Maharashtra or Tamil Nadu. The state had actually gone down the list of Indian states in terms of most human development indicators (in an early indicator of his tendency towards gaffes, then chief minister Modi said that poor malnutrition results for his state were due to girls dieting). Mr Modi's record as chief minister was sold on hype without much substance; he was elected prime minister as a consequence, and if he is re-elected in similar manner then we should not be surprised.

Nor are Mr Modi's actions as prime minister particularly surprising — with the major exception of demonetisation, of course. It is true that he has largely been statist in orientation, far from being the market-friendly reformist that many economists imagined in 2014. But, in fact, this is exactly what should have been expected. Mr Modi might have used the "minimum government" buzzword, but that was merely an early sign of his unmatched ability to use tokenism and slogans to appeal to multiple different groups of voters and influencers. In these pages in 2013, I looked through the then chief minister Modi's speeches and stated positions and found little of the reformer in them. Here is a short recapitulation of that. Most of us remember that CM Modi was the main obstacle for years to the passage of the goods and services tax for which PM Modi now claims credit. But there is more. CM Modi had, for example, argued that relaxation of foreign direct investment was meant only to benefit "Italian businessmen", a political — or personal — reference that is easy to categorise. He said that labour laws should be for states to change, not the Centre. He argued strongly against Manmohan Singh's rationalisation of diesel prices, saying that it was dangerous, and would cause India's "ship to sink". Limits on the number of subsidised gas cylinders imposed at the same time consisted of "cheating the people", according to CM Modi. And in case anyone is wondering what CM Modi's preferred approach was, his website said: "On the same day the UPA announced these regressive decisions [i.e., the fiscally responsible decision to decontrol diesel and limit LPG subsidies] Shri Modi announced 100 per cent relief on loans and 50 per cent relief on electricity bills for farmers."

At best, Mr Modi was a competent administrator of an already fast-growing state. He depended on his state's famously efficient bureaucracy and on personal relationships with big business that up his state's numbers through targeted investment. As some warned then, this is not a skill set that transfers easily over to the prime minister's office, where reform of administrative procedures and creation of capacity is a far more important task than micro-management of individual projects.

We should not therefore view this government as a disappointment. The prime minister's track record and statements prior to being elected were a fairly accurate predictor of how in fact the government has performed. It has, largely successfully, focused on infrastructure — for "building infrastructure is the real reform", according to CM Modi prior to 2014. It has largely depended on bureaucrats for policy innovation and implementation; it has avoided privatisation and indeed expanded the scope of the public sector by involving it in such things as supporting start-ups; it has built up liabilities, although much of that is off the balance sheet; it has centralised decision-making; it has reversed 25 years of external liberalisation by turning again to tariffs and industrial policy-style sectoral preferences. As happened in Gujarat, consumption growth — particularly rural consumption — has been below par.

As India enters another general election campaign, there should at least be an acknowledgement of how different expectations will have to be for another term from Mr Modi, which is the likely outcome of the vote. Economic transformation is off the table. It always was.

SBI makes a smart move

FINGER ON THE PULSE

T T RAM MOHAN

Should banks be linking their lending rates to an external benchmark? The Reserve Bank of India (RBI) seems to be having second thoughts on the subject. That has not stopped State Bank of India (SBI) from making its first move in this respect.

SBI has linked its rate on saving bank deposits and its rates for cash credit (CC) and overdraft (OD) to the repo rate. In both cases, this will be applicable to accounts of over ₹1 lakh. The saving bank deposit rate has been pegged at 2.75 percentage points below the repo rate (currently 6.25 per cent), that is, 3.50 per cent. The floor rate for CC and OD will be 2.25 percentage points above the repo rate, that is, 8.50 per cent.

Saving bank deposits account for 40 per cent of SBI's deposits, and 80 per cent of these deposits are valued at over ₹1 lakh. Thus, 32 per cent of SBI's deposits would be market linked. Corporate advances at SBI are 40 per cent of all advances. Even if we assume that 50 per cent of these advances are in the form of CC and OD, the latter would account for just 20 per cent of advances. In a declining interest rate regime, such as the one we are in, SBI's net interest margin would be favourably impacted by the move.

SBI's lending rates for other products (including housing loans) would be affected very modestly. These rates will be impacted through a reduction in the marginal cost of funds based lending rate (MCLR). The SBI move does not impact 68 per cent of all deposits and deposits are not the only sources of funds for banks. A 25 basis points (bp) change in the repo rate may translate into a change in the MCLR of about five or six bp. Complete transmission of the repo rate is possible only when banks can offer floating rates on term deposits. Indian depositors have shown no appetite for such a product.

Will other banks seek to emulate SBI? Well, some public sector banks (PSBs) may but private banks are unlikely to. For depositors, saving bank accounts at PSBs are about safety. These accounts are intended for transactions and not for returns. Not so the saving bank accounts at private banks. Unless the returns are attractive (relative to other investment opportunities), depositors would not want to risk their deposits with private banks. Besides, private banks need high deposit growth in order to sustain their higher rate of credit growth relative to PSBs in recent years. They are unlikely to want to drop interest rates on saving bank accounts.

SBI's offerings of CC and OD will now become very competitive. The move is smart because it will boost, not just the net interest margin, but SBI's market share in these products. If you are the market leader, you must act like one. SBI's move is a welcome sign that the consolidated giant is willing to do so.

Large exposure limit for banks

One other development in banking is worthy of note. The RBI is going ahead with its effort to limit concentration risk at banks. Banks and corporates had expressed their reservations after the RBI had made its Large Exposure Framework available for public comments in August 2016.

Effective April 1, 2019, banks' exposure to a single borrower will be capped at 20 per cent of tier 1 capital (present limit: 20 per cent of total capital). Banks' exposure to a group will be 25 per cent of tier 1 capital (present limit: 40 per cent of total capital).

The RBI's move bodes well for risk management at banks. The single biggest cause of higher non-performing assets at PSBs is neither corruption nor lack of competence in assessing credit risk, as is widely supposed.

Corruption is a constant in the system. It cannot explain the improvement in NPAs in the period 2004-08 or the huge build-up in non-performing assets (NPAs) consequent to 2013-14. As for skills in appraising credit risk, in many of the large NPAs in the system today, PSBs were members of a consortium that included private as well as foreign banks. The latter cannot be said to have shown superior expertise.

No, the fundamental failure of PSBs lay in managing concentration risk. PSBs got exposed to infrastructure and related areas to a greater extent than private banks. Private banks had a larger exposure to retail credit and, to that extent, were protected from the failures in the corporate world. The risk management committees of the boards of PSBs should have ensured that they stayed well within the RBI's exposure limits. They failed to do so.

The RBI has, no doubt, concluded that managing concentration risk is too important to be left entirely to banks. Its initiative could be hugely disruptive in the medium term. Banks will be forced to look for new business. Large corporates will have to source a larger portion of their funds from outside the banking system. Banks and corporates have their work cut out for them, but the RBI's initiative promises to make the banking system safer.

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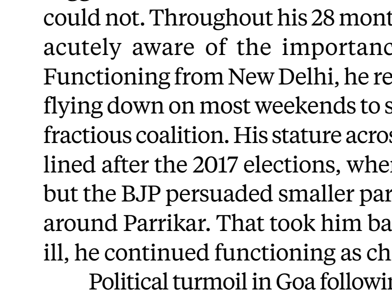
Heroes and their warts



KITABKHANA

T C A SRINIVASA-RAGHAVAN

Six years ago, I found myself in a Korean yoga ashram deep in some Korean hills. The guru there, a Korean lady, is my wife's friend. We spent three full days there doing nothing much, not even yoga. Even though it was early April it was still very cold. So I spent virtually all my time in the library which, apart from being well-heated, was also surprisingly well stocked in books in English.

One of those books was the controversial *Intellectuals* by Paul Johnson, a former editor of the *New Statesman*. It was first published in 1988.

I was hooked by the time I had reached the end of the first sentence, which reads as follows:

"This book is an examination of the moral and judgemental credentials of certain leading intellectuals to give advice to humanity on how to conduct its affairs." With that in mind, Mr Johnson lays bare the private lives and characters of guys like Rosseau, Shelley, Marx, Tolstoy, Bertrand Russell, Sartre etc.

What were they really like, he asks. Nasty or kind? Were they the grasping types, rattling their tin cups all the time? How did they treat their wives and children, born within and without wedlock? How did they treat people and friends? And their hygiene? Sexual preferences? Would any port do in a storm?

Mr Johnson says he has only set down established facts. What has resulted is, if I may coin phrase with an all too modest cough, "don't judge an intellectual by his thoughts alone".

Rosseau, Marx and Sartre

The biggest daddies of them all were Rosseau and Marx. Both devised blueprints for society that made kindness the basis of human and social relations. Both were implemented, which is what makes them great. But in private life these guys were weirdos.

Rosseau, says Mr Johnson, "led a life of failure, and of dependence, especially on women" but also on a series of patrons. He seems to have had, according to one of his employers, "a vile disposition" and "unspeakable insolence" apart from a "high opinion" of himself. He also wrote a book that was semi-porn which the Archbishop of Paris denounced for "insinuating the poison of lust". His love life was devoted to it. In short, horrible.

Marx, meanwhile, was "self-obsessed" and autocratic. Friedrich Engels, says Mr Johnson, observed that when Marx ran the periodical which he edited he did it like a dictator.

Above all, Marx had no time for democracy or elections. He "dismissed British general elections as mere drunken orgies." He thought the masses could not be trusted. He was always irritable, often angry, and hugely intolerant. Given to drinking a lot and eating spicy foods, he developed boils which "varied in numbers, size, and intensity... and appeared on all parts of his body including his bottom... and penis."

1873 he suffered a nervous collapse as a result. He had married a beautiful girl of Scottish descent called Jenny but could not look after her and the four or five children they had. He was always in debt, kept his family in hideous conditions and tended to oppress his daughters.

Fed up, his wife is believed to have said that she wished he would "accumulate capital instead of writing about it."

Another creep.

Russell and Tolstoy

This was the only chapter that made me wish I hadn't read the book. It is never nice to find that your god was a randy goat. This great mathematician, philosopher, pacifist and activist was a serial bedder-of-women. He just went on and on – and on and on from one woman to another. Their social status did not matter. I wonder, though, what it says about the women who went along. He seems to have been irresistible.

Then there was Tolstoy, a gambler and also a womaniser par excellence. Unlike Russell, however, he was willing to admit not just that but also to being a frequent victim of venereal diseases from the "customary sources". He told his biographer that he was going at it even at the ripe old age of 81, which was a whisker more than Russell.

I strongly suggest you read this book. It covers Hemingway, Ibsen, Brecht and even Victor Gollancz. And some others. A friend brought me copy from the US recently so that I could finish reading it. You can order it on Amazon, USA. Delivery is expensive but the book itself is now available for under five dollars.

Believe me, every rupee spent on it is well worth it.