

# Opinion

SATURDAY, MAY 18, 2019

## Rational Expectations

SUNIL JAIN

sunil.jain@expressindia.com  
@thesuniljain



## More support for I-regret-collegium

Justice JS Verma regretted his role in collegium-creation, Fali Nariman wished he never won & now Justice Kurian has regrets

**N**OT SURPRISINGLY, GIVEN how the sexual harassment charges against CJ Ranjan Gogoi were handled, to the allegations of intimidation of the complainant, the pendulum seems to be swinging away from the untrammelled power of the collegium, and towards the more consultative process envisaged by the National Judicial Appointments Commission (NJAC) Bill that the Supreme Court contemptuously struck down in 2015. Indeed, the power of the collegium has been abused so often, and for so long, the disillusionment set in quite some time ago.

The collegium taking over the appointment/transfer of judges from the government began with the First Judges case and got further consolidated in the Second Judges case in 1993. In 2009, Fali Nariman, who was one of those who won the Second Judges case, said he regretted winning the case since the collegium hadn't really lived up to expectations. And CJ JS Verma, the author of the main judgment also regretted this, arguing that what he had envisaged was not primacy of the judiciary in appointments/transfers, but a more effective government consultation with the CJ instead of just a token one.

The latest to say I-regret-the collegium is Justice Kurian Joseph who was one of the four judges who rejected the NJAC; only Justice J Chelameswar, who stopped attending collegium meetings as they were opaque/arbitrary, voted for NJAC. So, what was a 4:1 defeat could have become 3:2 if Justice Joseph had felt this way a few years ago, and who is to say this wouldn't have swayed another judge to make it a 3:2 NJAC victory? At a Vidhi Legal book-launch, Justice Joseph said that he was expressing his regret considerably faster — in under four years — than CJ Verma; while he was once optimistic about the collegium, he said, it had only got worse. Indeed, even as he agreed with Justice Lokur on how separation of powers in the NJAC judgment—between government and judiciary—“is the tectonic structure of the Constitution”, Justice Kurian had ruled “the present Collegium...lacks transparency, accountability and objectivity...The trust-deficit has affected the credibility of the Collegium...very serious allegations and many a time not unfounded too, have been raised”. In 2015, his judgment spoke of blatant violations, bad appointments, dictatorial attitude of the collegium, etc, but at that point, he felt, “to me, it is a curable situation yet”.

Ironically, such is the CJ's complete power, much of what Justice Gogoi accused then CJ Dipak Misra of doing—in that famous press conference along with three other judges—such as presiding over benches where he had a self-interest, were things he repeated as CJ; he presided over the first bench that discussed the sexual harassment allegations, and even said this was part of a larger conspiracy to hobble him.

While the four judges raised the issue of judicial corruption—including allocating cases to certain benches— with then CJ Misra, they also spoke of Justice CS Karman who gave a list of 20 corrupt sitting/retired Supreme Court and high court judges. While the letter of the four judges spoke of the need to “revisit the process of appointment of judges and to set up a mechanism for corrective measures other than impeachment”, no action was taken under CJ Gogoi. Indeed, even after the bribery charge against Justice Nirmal Yadav of the Punjab and Haryana High Court, she was only transferred to another court and her case is still pending after a decade; there has been no proper investigation of the charges made against judges—including the then CJ—by former Arunachal Pradesh chief minister Kalikho Pul in his suicide note. Some of this falls under the Judicial Standards and Accountability Bill that was brought into Parliament in 2010—it was to have a National Judicial Oversight Committee, a Complaints Scrutiny Panel and an Investigation Committee—but it got scuttled.

While collegium-supporters feel judicial independence is part of the Constitution's basic structure, and that consultation with the CJ means concurrence—which is how the CJ has the last word—Justice Chelameswar said this was not the case in countries like the US and the UK; in the US, the president appoints judges with the advice and consent of the Senate. And while the proximate cause for the collegium was the government riding rough-shod over the judiciary, Justice Chelameswar pointed out that the transfer of 16 high court judges by the President in 1976 was done in consultation with the CJ. He records how “of 53 appointments of Judges to some High Courts made in 1984-85, 32 were made on the recommendations of acting Chief Justices...it is believed that the senior most Judges of some High Courts (from where the said 32 recommendations had originated) who initiated those recommendations as acting Chief Justices, were made permanent Chief Justices only after they agreed to recommend names suggested by the Executive”.

And, on the issue of the independence of the judiciary being part of the basic structure of the Constitution, Justice Chelameswar quotes BR Ambedkar as saying, “it would be dangerous to leave the appointments to be made by the President, without any kind of reservation or limitation, that is to say, merely on the advice of the executive of the day” and that “to make every appointment which the executive wishes to make subject to the concurrence of the Legislature is also not a very suitable provision”. And yet, Ambedkar says, “to allow the Chief Justice practically a veto upon the appointment of Judges is really to transfer the authority to the Chief Justice which we are not prepared to vest in the President or the Government of the day. I therefore, think that that is also a dangerous proposition”.

The current crisis in the SC will blow over, especially if the judges close ranks, as they did after CJ Misra retired. But till there is untrammelled power for the Collegium and the CJ and there is no independent mechanism to investigate/sack corrupt judges, the crisis will keep reappearing. The latest cases—three of them within the space of a few months—where SC orders were changed by lower functionaries are yet another symptom of this.

## GenderGOOGLY

Some Bengaluru colleges are punishing girls for better performance by posting higher cut-offs for them vis-a-vis boys

**I**T IS RATHER unfortunate that some colleges in Bengaluru are fixing higher cut-offs for girls for admission into pre-University (PU, or +2/XI-XII) because girls have performed better than boys, and the colleges fear that a flat cut-off would mean that girls will significantly outnumber boys in the colleges, affecting “gender balance”. This is nothing but punishing girls for performing better. The irony is that the proponents of this “affirmative action” are citing an order of Karnataka's department of pre-university education that was meant to encourage colleges to admit more girls—the department had asked colleges to follow an equal number of girls and boys seat-matrix to ensure more girls were given admission. The order did not specify anything on posting separate cut-offs.

In Bengaluru's reputed Christ Junior College, the science cut-off for boys and girls is 94.1% and 95.1, respectively, while in MES PU College, it is 92% and 95%! Similar cut-offs have been posted for the arts and commerce streams, too. Affirmative action is based on historic and continuing social disadvantage. While women have suffered such disadvantage in a deeply patriarchal set up—a reason why there were fewer women in colleges—by no stretch of understanding can boys be considered disadvantaged in the particular case. Each individual case may vary, but as a norm, boys would have received the same opportunities to learn. Also, in the face of any fear of boys being left behind by girls, the focus should be on creating more infrastructure. When nearly every expert sees greater participation of women in the labour force as key to future growth, stunting them at the start is a cardinal sin.

## ● RATE OF PROGRESS

FROM JANUARY 2015 TO JUNE 2018, THERE WERE SEVEN REDUCTIONS IN THE REPO RATE, AMOUNTING TO 200 BPS, AND BANKS' WALR CHANGED BY 205 BPS DURING THE PERIOD

# Banks have been transmitting rate cuts

MADAN SABNAVIS

Chief economist, CARE Ratings  
Views are personal



**A**RE WE BEING unfair when we constantly fret over the slow transmission of interest rates by banks when the repo rate is cut? This has become a habit of late, one where there is a lot of concern raised on the slow transmission process. The storyline is now familiar. RBI lowers the repo rate and is joined by the government which presses banks to take action on lending rates. Periodically, bankers are summoned to Delhi, and the case is put forward on lowering rates. The view put forth by economists and analysts is that the banks are not following RBI's suit, and that blunts the efficacy of monetary policy. How far is this true?

Two things need to be understood here. The first is that the lending rate is driven by a formula. There is the base rate and the MCLR (an improvement over the base rate concept), which is driven by a formula. One variable in the formula is the repo rate; that, however, affects a very small part of the total cost of funds and is negligible (total LAF borrowings at repo rate is fixed at 1% of NDTL). The most important component is the deposit cost, which has to change. If this cost changes, the base rate or MCLR will come down accordingly. This becomes the benchmark for banks to decide on other lending rates. Therefore, the crux is the changing of the deposit rate and the benchmark lending rate.

The second is that the mechanics of interest rates changes. Banks first have to lower deposit rates. But all deposits are generally contractual and have fixed rates till maturity. Hence, when it comes to time deposits, the new price can come in with a hiatus, say, when the deposits come for renewal or when new deposits are reckoned. Therefore, even if deposit rates are lowered, the impact on cost would come with a lag. Now, when it comes to lending rates, once

lowered, it would be applicable for all loans and, hence, the revenue would dip for the bank when rates are reduced. Hence there is a priori reason to believe that the pace of lowering of lending rates will be calibrated with time. But what is the true picture?

The accompanying graphic looks at the changes in interest rates developments since January 2015. The movements in the repo rate are mapped with the changes in the extent to which the WALR (weighted average lending rate) on fresh rupee loans sanctioned has moved.

The idea here is to look at the month in which the repo rate was changed and see the corresponding change in the WALR during the period when the new repo rate change was valid, which would be till the next change in policy was announced. From January 2015 to June 2018, there were seven reductions in the repo rate (six occasions of 25 bps each and one of 50 bps), amounting to 200 bps, and the weighted average lending rate (WALR) of banks changed by an equivalent of 205 bps during this period. This indicates an elasticity factor of 1. When the repo rate was increased by 50 bps in the next two policies, the WALR for banks rose by 51 bps, which is again an elasticity of 1. Therefore, if one tracks the changes on the repo and the reaction of banks to these changes, it does appear that banks have been very receptive to policy. There is little reason to believe that there is any transmission issue with banks.

The change will not be instantaneous for sure and will take time to

work out, as can be seen in the graphic. There are processes involved in the bank where the ALCO meets and decides on the interest rate action. In fact, when the rate-cut is allowed to work through for a longer period of time, which can be more than six months, then the effect is sharper and the past rate-cuts also get included in the final impact. This has been so in all the three instances when the WALR has changed by more than 40 bps over the longer time period. In two of these cases, the reaction was to an immediate cut of only 25 bps—in October 2016 and August 2017.

Hence, quite to the contrary, it appears that banks have actually been very receptive to RBI's policy changes and passed on the benefit of lower repo

rates to the customers. This does not appear apparent when one looks at just the base rate or MCLR that have tended to be sluggish in changing as they are driven by the formula where the deposit rate is critical. This is probably why it does look as if banks lower their deposit rates at a faster pace than their lending rates. But, as the data shows, this is not true and banks do in fact give a good part of the benefit to the average customer. In fact, one could argue that banks have been doing so even though the NPA levels have been high, where the credit risk environment has not been congenial. Ideally, these rates should be less than elastic when the credit risk perception is higher.

This data should also satisfy RBI that has been trying to reconcile the phenomenon of repo rate changes with market interest rates. In a way, it is a vindication of the efficacy of monetary policy. Data, however, indicate that the interest rate cut should be given time to work through and, typically, a longer time-period relates well with policy changes. There is definitely no need to get overly critical of bank reaction to policy changes.

### Change in repo

	Quantum of change	Period of new repo rate	Quantum of change in WALR
Jan 2015	-25	Jan-Feb 2015	-17
March 2015	-25	Mar-May 2015	-22
June 2015	-25	Jun-Aug 2015	-9
Sep 2015	-50	Sep'15-Mar 2016	-50
Apr 2016	-25	Apr-Sep 2016	-12
Oct 2016	-25	Oct 16-Jul 2017	-55
Aug 2017	-25	Aug 17-May 2018	-40
Jun 2018	+25	Jun-Jul 2018	+23
Aug 2018	+25	Aug 18-Jan 2019	+28
Feb 2019	-25	Feb 2019	-12
Apr 2019	-25		

Source: RBI

## Don't drag India into a trade war

For the US to be a stakeholder in India's future, trading some short-term gains for more important long-term returns is implicitly required

ATMAN TRIVEDI

Bloomberg

First China. Now India? In recent months, US president Donald Trump has made clear that the trade war will reach beyond the People's Republic. Not only has he threatened Japan and Europe with import duties on cars, he's repeatedly blasted India as “the tariff king”.

Trump has obsessed over the Asian giant's high levies on Harley-Davidson motorcycles and complained about its modest \$24.3 billion surplus in trade with the US. In March, the president gave Congress notice that he plans to terminate duty-free privileges for \$5.6 billion worth of Indian exports to the US. He could do so at any moment.

And Trump may not stop there. His administration is toying with the idea of exercising the same legal authority used to levy unilateral tariffs against China to impose higher duties on India. Imagine the world's largest democracy, which Washington has diligently sought to enlist as an ally against Beijing, being lumped together with America's main strategic competitor.

India represents the rare bright spot in US foreign policy. With much difficulty, a years-long, bipartisan effort has greatly deepened ties with the prickly emerging power. Once considered the ultimate swing state, India is now seen as the fulcrum of the White House's Asia strategy.

Trump's trade tactics appear to reflect a belief that the US can fight tooth-and-nail with friends such as Europe and Japan without jeopardizing broader strategic ties or undermining efforts to balance China. Even in the unlikely event he's right, given that those longtime allies count on the US security umbrella, that's hardly a winning play in India.

The country hasn't entirely shed a post-colonial mindset; it fervently values its autonomy and its place as a

non-aligned nation. Regardless of how powerful strategic ties have grown in recent years, India still has no interest in a formal alliance with the US.

Successive US administrations have generally been willing to respect India's choices. At the same time, they've quietly labored to strengthen habits of cooperation. Through a series of actions—in particular a civilian nuclear agreement reached in 2005—these administrations have effectively declared: “India's rise lies in America's interests.”

If frictions were now limited to trade, those common interests might provide enough glue to maintain this positive momentum. Instead, the Trump administration's complaints have expanded to include demands that India cut oil imports from Iran to zero and abruptly end significant arms purchases from Russia, or else face sanctions. The president has even belittled India's significant development contributions in Afghanistan.

All this only reinforces the suspicions some Indians still hold about US reliability. Being a stakeholder in India's future implicitly requires trading some short-term gains for more important long-term returns. The Trump administration should remember that an economically vibrant India will also be a much more capable strategic partner.

A hasty step such as removing developing-nation trade benefits, on the other hand, could begin to undermine the core logic of the partnership. Whatever government emerges from Indian elections that conclude later this month may well decide it

has little choice but to respond with retaliatory duties.

This would run counter to India's own interests, of course. A trade confrontation with the US would undermine its argument that global companies should choose its huge, young, tech-savvy market as an alternative to China. Foreign investment is crucial to helping India develop its economy and play a more robust regional role.

It's also worth pointing out that Trump is not entirely wrong. India is in need of trade reform and could have taken useful steps after Washington launched an April 2018 investigation into its practices and before the onset of the current political season. Instead New Delhi made scant progress and even slid backwards. The new government should swiftly revisit illiberal trade policies that hamper India's regional economic integration, exports, global competitiveness and labor productivity.

A number of those policies are actually designed with China in mind. Like the US, India runs by far its largest trade deficit with its wealthier neighbor. If just afforded a chance, it might quietly lend a hand to US efforts to change China's trade approach.

The Trump administration should give Indian leaders at least a couple months to get organized and draft some serious proposals, including on e-commerce restrictions. While the US dukes it out with China, India can hopefully get its act together and give Trump less incentive to launch another ill-advised trade assault.

This column does not necessarily reflect the opinion of the editorial board or Bloomberg LP and its owners

## LETTERS TO THE EDITOR

### BJP loses its moderate guard

It is sad that in this day and age we are expending our time and energy on discussing whether Mahatma Gandhi's assassin Nathuram Godse was a terrorist or a patriot. Things have now come to such a pass that a candidate fielded by India's ruling and principal party could openly hail Godse as a desh bhakt. One man's terrorist is not just another man's freedom fighter, but also a patriot, it would seem. Pragya Singh Thakur's unabashed glorification of Godse was clearly beyond the pale. Still several BJP leaders are unapologetic about her eulogizing Godse. One BJP leader described Mahatma Gandhi as the Father of Pakistan. Another leader said if Godse killed one person, Rajiv Gandhi killed thousands, 1700, to be precise. Thankfully, Sadhvi agreed to toe the party line of respecting Mahatma Gandhi and refusing to extol Godse as a patriot. BJP was under political compulsion and pressure to extract an apology from the saffron-clad “firebrand” leader. Be that as it may, it is hard to comprehend why a patriot should kill or want to kill another patriot or compatriot. To her credit, Sadhvi did not say that Mahatma Gandhi was not a patriot. While Sadhvi was honest enough to say what she felt about Godse, most of her party men are hypocritical. They share her view of Godse, still maintain a strategic silence condemn one among their number for fear of public anger. The glorification of Godse by a person who prospered in BJP tells us something about the party and its virulence. Despite the claimed divergence between her “personal view” and “party view”, Sadhvi certainly represents Sangh Parivar's world-view or else she would not have risen to her present “stature” and “fame”. With the take-over of BJP by the Modi-Shah duo, the moderates in the mould of Vajpayee in what is essentially a Hindu right-wing party have become extinct. — G David Milton, Maruthancode

● Write to us at feletters@expressindia.com



# The many facets of Sino-US trade dispute

The bottom line is that Xi Jinping may have provoked the dispute, departing from the dictum of China "biding its time" before its time—a cumulative backlash to China's actions in Taiwan and North-east Asia, and the South China Sea

**ANURAG VISWANATH**

The author is a Singapore-based Sinologist, and adjunct fellow at the Institute of Chinese Studies, Delhi. Views are personal



**E**CONOMICS IMPACTS POLITICS—and the other way round—is equally true. Eleven rounds of the Sino-US trade talks led by China's Vice-Premier Liu He (an economist) in Washington DC failed to reach a trade deal, with the US increasing tariffs on \$200-billion worth of Chinese goods from 10% to 25%. Tariffs on the remaining \$325-billion worth of goods at that rate are to follow. Despite US President Donald Trump's warning, China has retaliated with a tariff hike of 5% to 25% on \$60-billion worth of US goods. While China has respected the retaliatory measures in terms of respect and dignity, the American tariffs go well beyond the economic dimension. In fact, the American response appears as part of an evolving strategy that takes a long-term picture of China as an economic and strategic rival. Clearly, the trade dispute has multiple dimensions.

On the other hand, China views that tariffs and other measures from the US, not 'enforcement mechanism', are the key issues. China appeared to have agreed to an 'enforcement mechanism' but backtracked, the reason why the US says China reneged on negotiations. Instead, China supports a nuanced 'regulatory mechanism'. While legislation would be enforceable and transparent, a 'regulatory mechanism' would work differently, where the Communist Party (CCP)/state could work it to advantage on an 'on and off' basis. The Chinese themselves may not be necessarily opposed to 'regulatory mechanism' as they view the CCP as the reincarnated Confucian 'paternal state'/'emphorship of yore' that upholds the 'mandate of heaven', and national interests rather than personalistic interests.

There is ample writing on the wall to suggest that the here and now matters much less than the American long-term strategic interests. The recent statement by the US Secretary of State, Mike Pompeo—that of China posing a challenge of "an authoritarian regime that's integrated economically into the West in ways that the Soviet Union never was"—is an inkling of how the US views China: Somewhat of a formidable combination of the politics of the Iron Curtain with the economics of the Japanese miracle. This constitutes the backdrop to the Sino-US trade talks.

That said, the American tariffs go well beyond the economic dimension and should be understood in the context of China's rise and recent actions. China's territorial claims in the East and South China Sea, land reclamation, military facilities and maritime militia in the South China Sea have caused concern. In a striking departure, British and French ships have joined the Freedom of Navigation Operations (FONOPS). Recently, India participated in naval exercises with the US, Japan and the Philippines in the South China Sea.

The US has cited China reneging on negotiations where the 'enforcement mechanism' remains a point of contention. The US has been trying to pin China down to legislation—regulations and laws embedded in the legislative process aimed at curbing forced technology transfer and intellectual property protection, rather than have the continued scenario where foreign companies are welcome into China but have to partner with local companies, which forces transfers.

Other key differences between the US and China include Taiwan and North-east Asia (North Korea), areas where China challenges the primacy of the American 'pivot'. On Taiwan, China feels a national anxiety underpinned by a feeling that time is running out for reunification. This has to be understood in the context of Taiwan's demography. Taiwan has a population of 23.7 million and 40.7

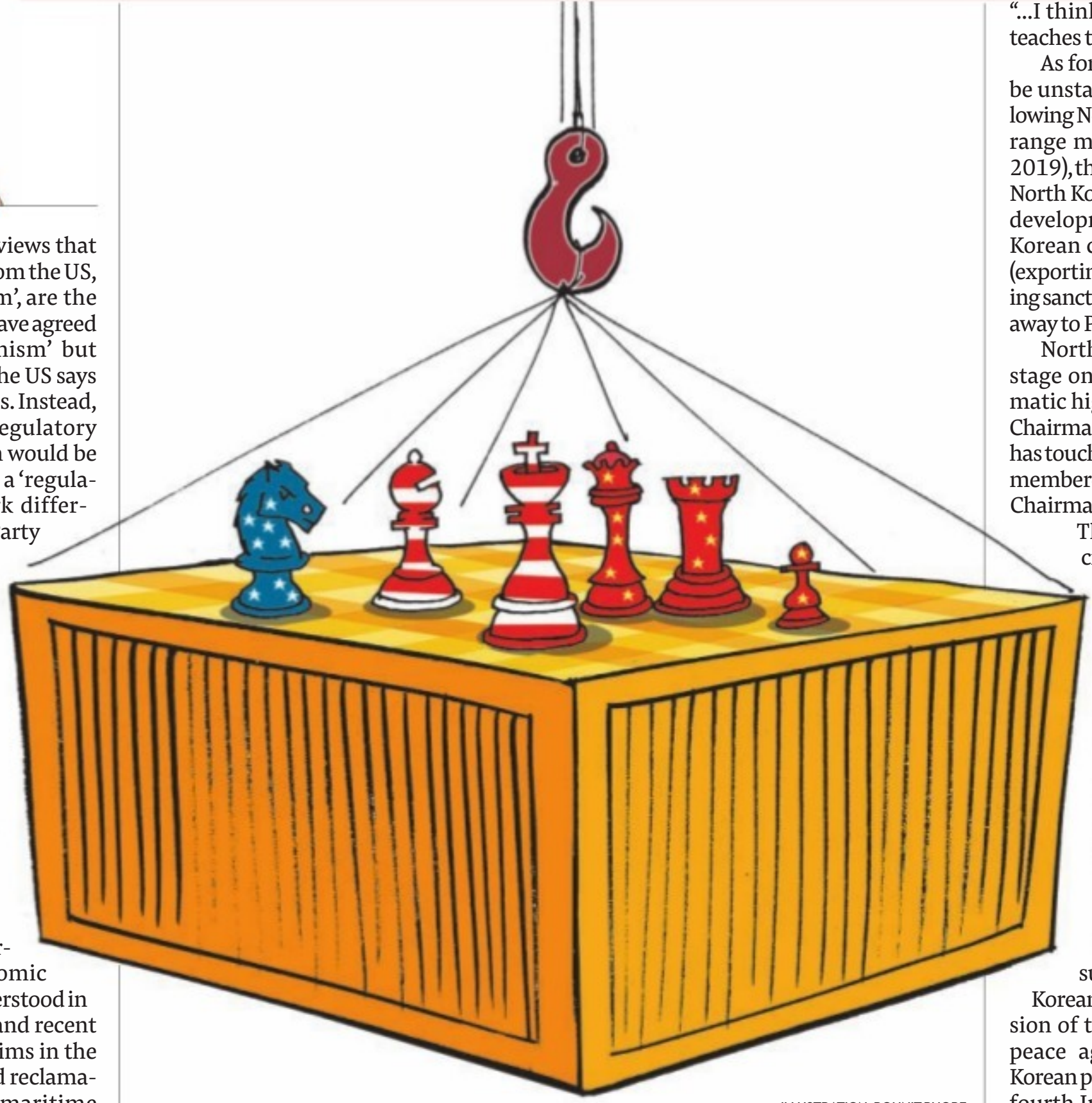


ILLUSTRATION: ROHNIT PHORE

**While it is a forgone conclusion that both the US and China will be affected by tariffs, China will be more so. In the US, the load of tariffs will impact US importers and indirectly impact consumers who now have to pay more for Chinese goods. For the Chinese, the tariff hike shows that President Trump is no 'paper tiger'**

is the current median age. Those aged 65 and above will make up 20% of the total population by 2026. In other words, the post-1949 generation (born and brought up in Taiwan) is increasing, and the older generation with memories of China and

the emotional impulse of reunification is decreasing. Instead of reunification, Taiwanese President Tsai Ing-wen, who faces re-election (January 2020), has called for support of Taiwan's democracy, tellingly saying:

"...I think the experience of Hong Kong teaches the Taiwanese a lot."

As for North-east Asia, it continues to be unstable, with renewed tensions following North Korea's resumption of short-range missile tests (May 4 and May 9, 2019), the first missile launches since the North Korea's ICBM in 2017. In a parallel development, the US has seized North Korean cargo ship named Wise Honest (exporting North Korean coal) for violating sanctions. Wise Honest has been towed away to Pago Pago, American Samoa.

North-east Asia has gained centre stage once again, given that the diplomatic high following President Trump-Chairman Kim summit (Singapore, 2018) has touched a new low—following the dismembered talks at the President Trump-Chairman Kim summit (Hanoi, 2019).

The optics in North-east Asia is critical, given that it is the last bastion of the Cold War between China, North Korea, and the US, South Korea and Japan on the other.

Much of the enthusiasm surrounding the 4.27 Panmunjom Declaration (April 27, 2018), which marked the first Inter-Korean meet in a decade, has dissipated. The key Panmunjom Declaration and Unification of the Korean Peninsula at Panmunjom (the first Inter-Korean meet) that affirmed the conversion of the armistice agreement into a peace agreement and a nuclear-free Korean peninsula is yet to materialise. The fourth Inter-Korean meet is yet to take place. On ground, UN operations have stalled DMZ Tours to Panmunjom at the DMZ (Demilitarised Zone).

The US has been frustrated that sanctions on North Korea have had limited impact on North Korea, given that for China and Russia, North Korea is a 'core interest'. North Korea has been holding up, despite being in the midst of what the UN estimates a severe 'hunger crisis'. Ten million North Koreans are at risk after a bad harvest, with the 2018-19 food crop production 4.9 million metric tonnes, the lowest since 2008-09. The food deficit is estimated to be 1.36 million metric tonnes.

The South China Sea and North-east

Asia speak volumes about the niggling issues festering in the US backyard, whilst Sino-US talks are out in the front yard.

While it is a forgone conclusion that both the US and China will be affected by the tariffs, China will be more so. In the US, the load of the tariffs will impact US importers and indirectly impact consumers who now have to pay more for Chinese goods. The US may tilt towards a 'better late than never' approach.

For the Chinese, the tariff hike shows that President Trump is no 'paper tiger'. Despite the hoopla surrounding Sino-US trade talks (or even the summit meeting with Chairman Kim in Hanoi), Trump has walked away, holding the line. This is a departure from the previous decades when China was given leeway, when it was weaker. Trump's stance may have a favourable bearing on his re-election bid in 2020.

On China's part, reactions to the tariffs have been low-key and, if anything, have been downplayed by the official media. China's commerce ministry has said that 'necessary counter measures' will be taken. Vice-Premier Liu He has sought restraint on both sides and need to nip 'unlimited escalation' in the bud likening the talks to 'running a marathon ... that gets harder as you reach the final stages'.

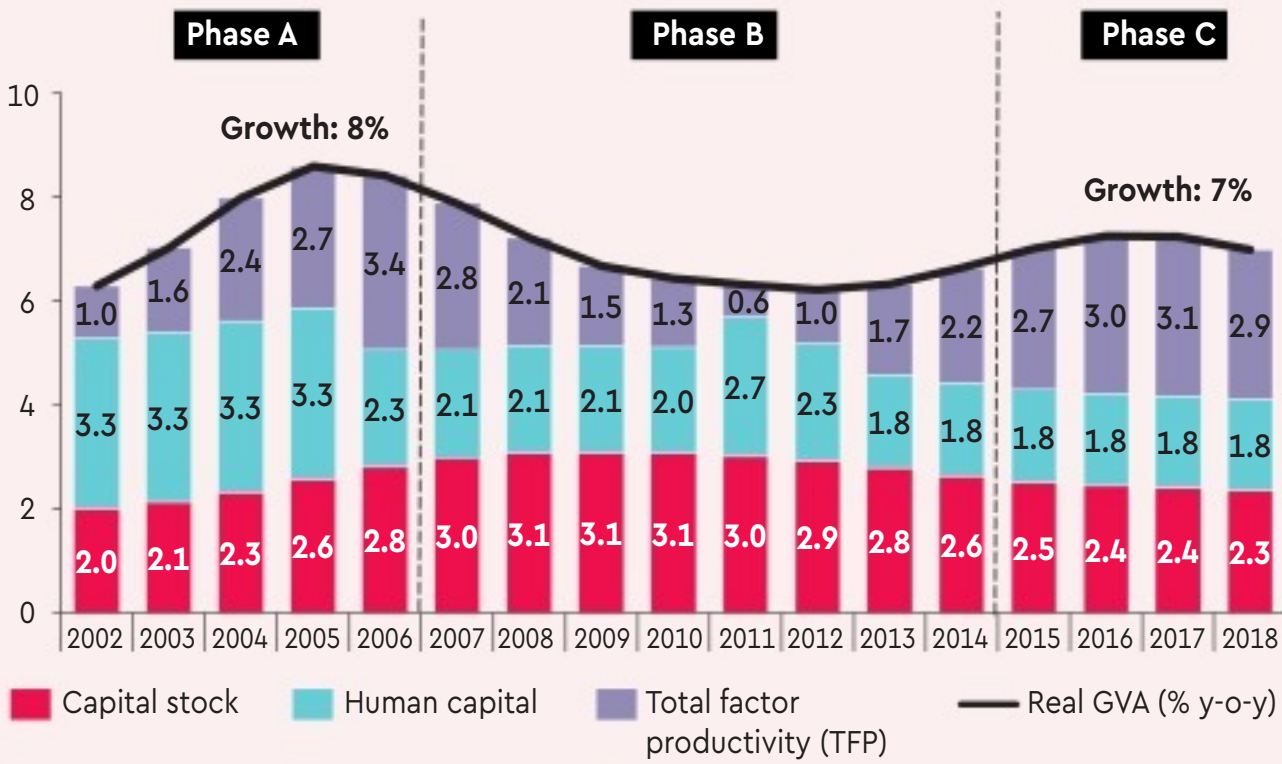
Chinese media is showing restraint, too. The *People's Daily* (Communist Party's newspaper) carried an article saying the US had "misjudged China's strength, capacity and will, further escalating trade friction between our two countries." The *China Daily* 'deeply regrets' the tariff hike, running a collection of comments by global analysts on the implications of the tariffs. Even the *Global Times*, known for its acidic tongue, showed uncharacteristic restraint, saying that 2019 marked 40 years of Sino-US relations and that "at 40, one should no longer be confused." China is not blowing its own trumpet about the retaliatory tariffs either.

Despite the lowbrow, low-key, muted criticism of America and, importantly, the absence of criticism about China's own political leadership, there is little escaping political damnation. In China, where 'face' (*mianzi* or 'keeping face') is key, China seems to have 'lost face' in the global order. Has China erred in judgement and made a miscalculation—of departing from the dictum 'biding its time' before its time? That is the question that Zhongnanhai must ask itself.

## DATA DRIVE

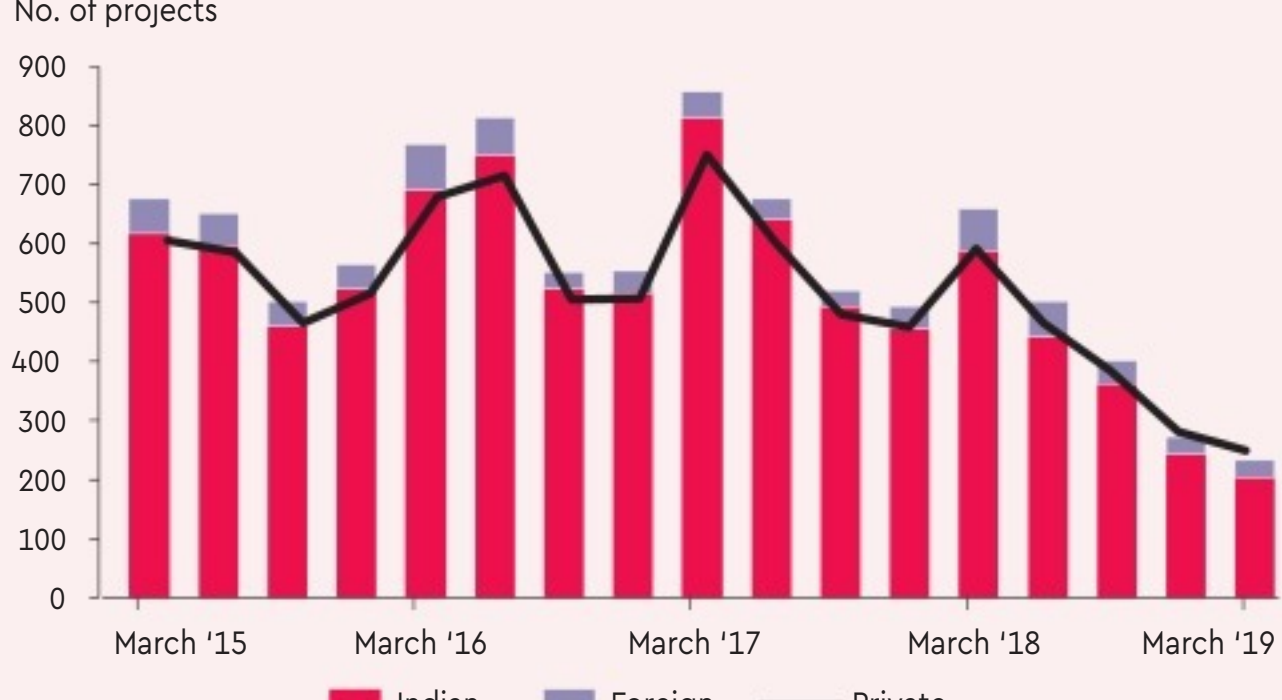
### India's growth curve: TFP peaked in 2006

(Contribution of inputs to GDP growth; ppt contribution)



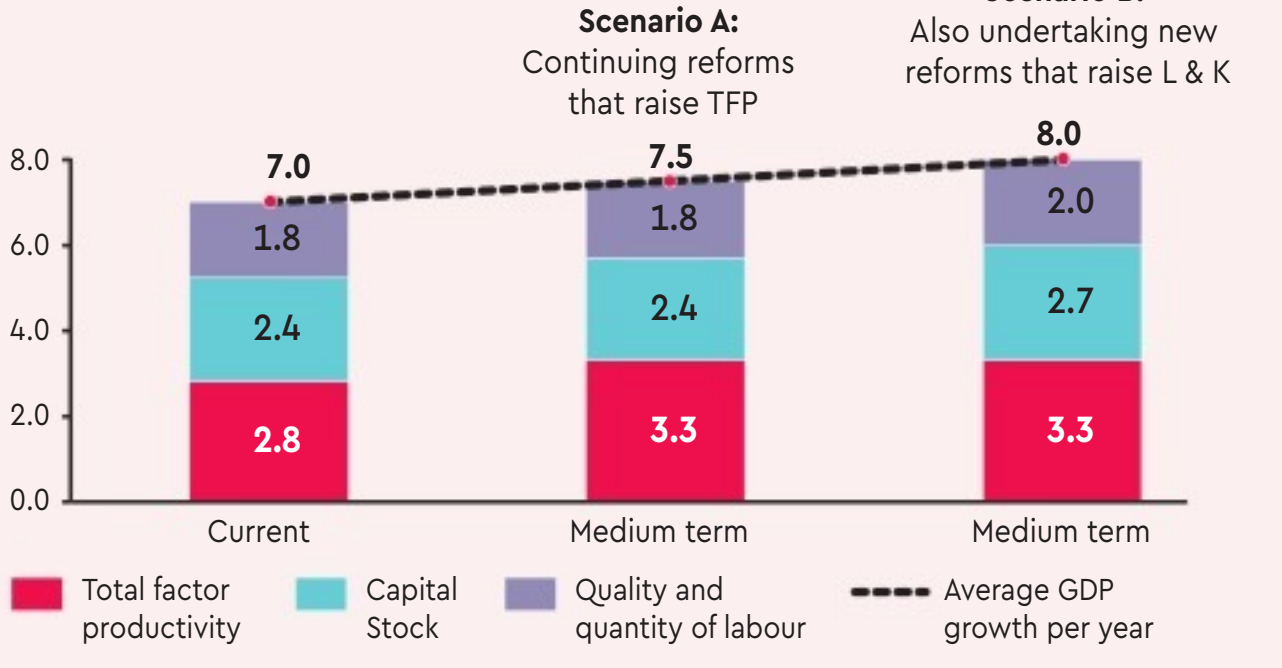
### Private investment remains weak

(Flow of new investment projects in the private sector)

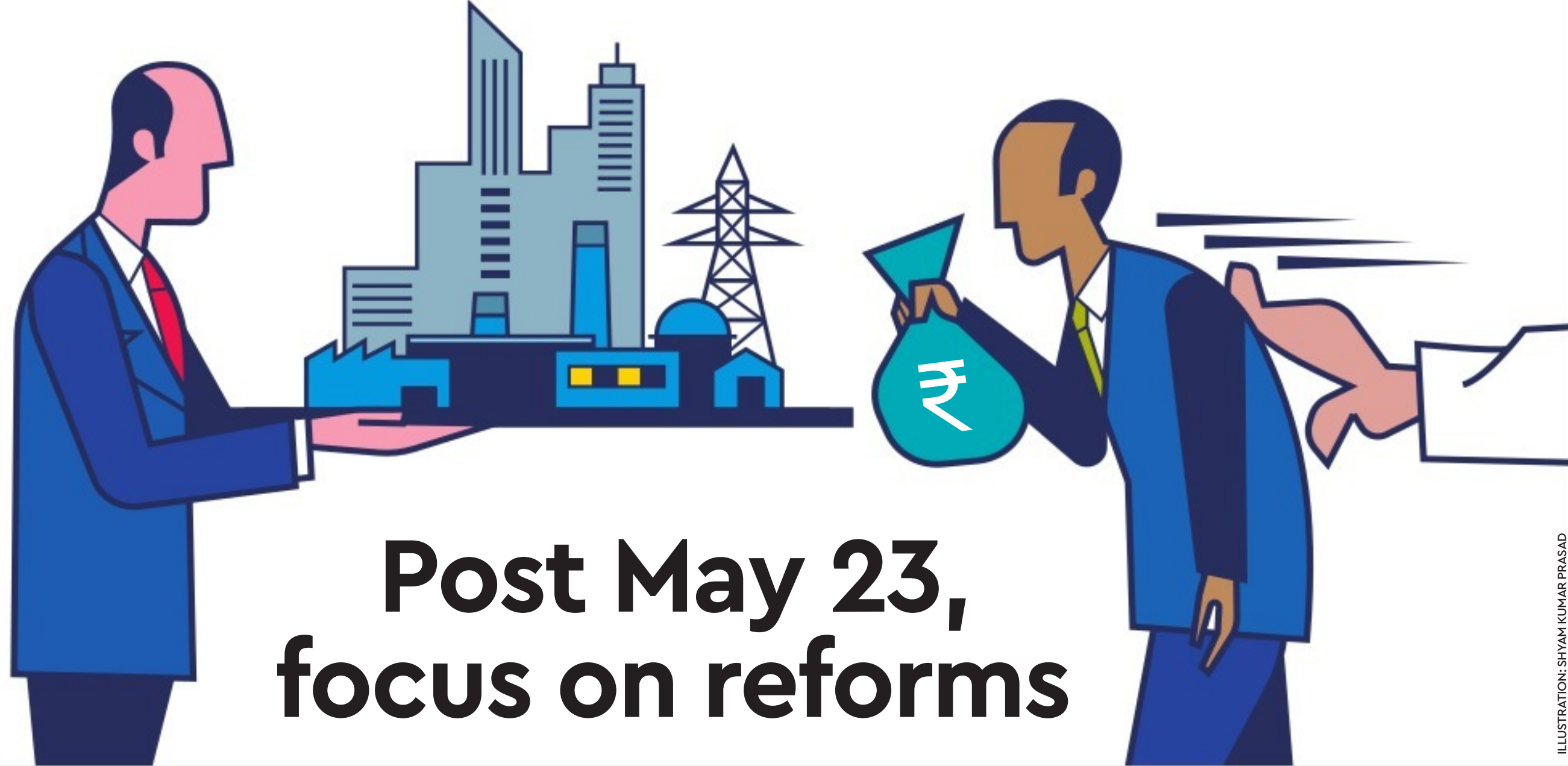


### Augmenting labour and capital is critical for raising India's potential growth

(Contribution of inputs to GDP growth; ppt contribution)



Source: HSBC, CSO, RBI, Budget documents



## Post May 23, focus on reforms

**A**FTER THE ELECTION results are announced on May 23 and a new government at the Centre is formed, the focus must shift towards the reform agenda. As gross domestic product is assumed to be produced by combining physical capital and human capital at the economy's overall level of productivity or total factor productivity, pushing up growth from 7% to 8% would require reforms that augment capital and labour. A report by HSBC says that the period from 2004 to 2006 reported a spurt in total factor

raising India's potential growth. Strong global liquidity and growth too helped, which pushed up India's potential growth level to 8%.

After the global financial crisis in 2008, India's growth started falling and all drivers of growth—capital, labour and total factor productivity—were weakened considerably. Growth performance since 2015 has been different as the drivers are no longer moving in tandem. The report points out that the growth in the capital stock is falling, reflected in the decline in investment rate. Gross fixed capital

formation dropped to 28.6% of GDP in FY18 from an all-time high of 34.3% as private sector investment remained stagnant at 11% of GDP during the period. Household investment, which accounts for small and medium enterprises, reported a steep fall—from 15.7% of GDP in FY12 to 10.3% in FY18.

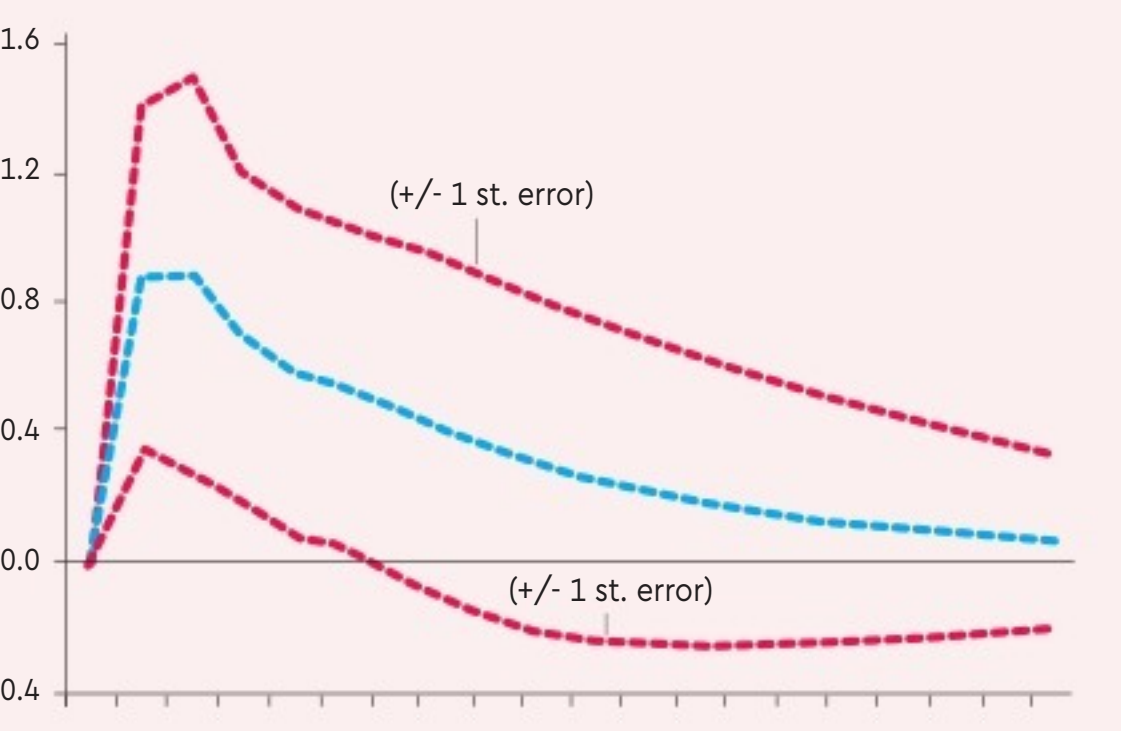
The report underlines the fact that even if the new government does not undertake any new big reforms, but simply focuses on recently enacted ones like GST, IBC and digital payments to settle down, potential growth could

rise from 7% to 7.5% through impact on total factor productivity.

In order to raise public investment in a fiscally responsible way, the government needs to raise revenues. Disinvestment, improving GST structure, enacting a new and improved Direct Taxes Code and monetising land holdings can help in raising funds. Higher fiscal revenues, the HSBC report says, will give some leeway for raising public, and thereby private investment, as higher public investment tends to crowd in private investment in the country.

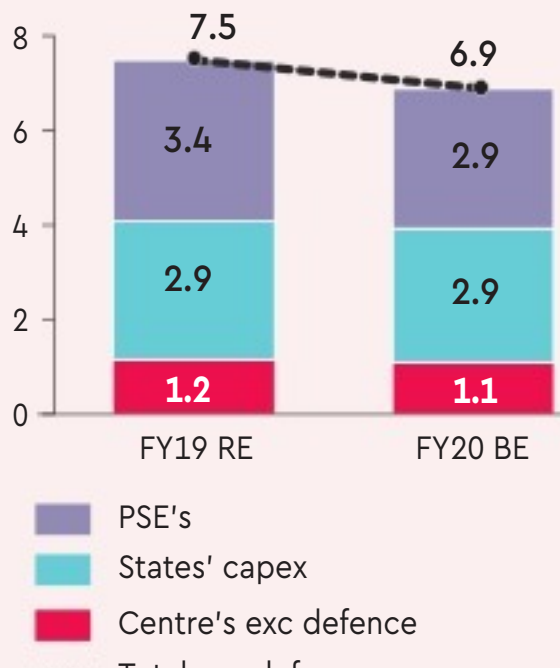
### Public investments crowd in private investment

(Unit response of all new private projects to one unit rise in all new public projects)



### Public sector's spend on capex is likely to fall

(Capital expenditure; % GDP)



### Public sector is using an elevated borrowing programme

(Gross market borrowings; % GDP)

