Splitsville in India Inc

Differences over culture, management and focus is making even many supposedly "happy" partnerships come unstuck

ACROSS THE BOARD

SHAILESH DOBHAL

Years ago, a fairy large business owner told me in the course of an interview that the biggest learning for her from a failed joint-venture in a related business was never to get into bed in business with anyone, because sooner or later the partners always pull in different directions. The excuse could be differing views on strategy, finances, control, culture or even something like personal chemistry.

Scanning the headlines in the last fortnight or so brought her prescient words back to me. Splitsville seems to be playing all over again in India Inc., albeit at different stages and often in stealth. After staying put for six years and investing ₹4,500 crore, and taking executive charge of the financial conglomerate Shriram Group, Ajay Piramal is looking to exit the group lock, stock and barrel. Serial entrepreneur and investor V G Siddhartha exited his investment in mid-tier IT firm Mindtree triggering off a takeover battle with Larsen & Toubro. IndiGo promoters' fight over who gets to control board and management appointments is all out in the open. And for all the other problems around a failed business model, what also added to Jet Airways' closure was the sheer distrust between promoter Naresh Goyal and his foreign partner, the Abu Dhabi-based Etihad.

It is not that India Inc is stranger to divorces. Far from it. In fact, the path from the 90s is littered with splits across sectors — from Godrej-Procter & Gamble, Britannia-Danone, Birla-AT&T-Tata, Hero-Honda and many such. What marked these earlier partnerships was the need for the foreign partner for someone to help navigate the bureaucratic and political labyrinth in India. Once these controls were relaxed and made simpler by the government, there was no reason to carry on with the Indian partner. And often it was the foreigner who pressed for the separation and picked a big separation bill.

In that sense, the current spate of divorces or near-divorces is different. They involve partners with supposedly complementary skills, and not necessarily driven by regulatory need to have a partner, barring Etihad which can't invest more than 49 per cent in an Indian airline and perforce has to have an Indian as the majority partner.

Piramal was supposed to bring in the moolah and the management smarts to steer a traditional group with no clear succession plan to bigger things, so much so that the founder even willingly gave up the executive head's position. Apparently, it was the culture issue, where Piramal was seen as an outsider, with an aggressive business approach that did not sit well with the conservative south India-based group. Now the separation, according to founder R Thyagarajan, is made out to be a purely financial move to exit with a good return! A new partner hunt is on at Shriram, with marquee private equity and business group names being thrown around.

Again, the partners at IndiGo — Rahul Bhatia and Rakesh Gangwal — complemented each other, one with money and deep knowledge of the Indian business ecosystem and the other with decades of global airline experience right at the top of the food chain. They even split the shareholding almost equally, but sewed up an apparently one-sided contract which has become the bone of contention between the two at the country's biggest and by far the most successful airline.

The two partners at Mindtree — V G Siddhartha and the management team led by Subroto Bagchi — essentially differed on how they viewed the firm's future. Siddhartha saw better value for his investments by subsuming Mindtree in the bigger L&T fold, whereas Bagchi and team made it a culture issue for staying independent. And even though it was the firm's largest shareholder, Siddhartha, who invited L&T to come and pick up his stake in L&T, the ensuing fight was billed wrongly as a hostile takeover.

At Jet, the foreign partner made Goyal's complete exit a pre-condition to even think of rescuing the financially troubled airline. Little wonder it is now reportedly in talks with the Hinduja Group to restart the airline.

In the pits despite a rally

Skewed trade policies are preventing domestic iron ore miners from taking advantage of the rally in global prices despite a surge in pithead stocks

KUNAL BOSE

That Indian iron ore exports would once again be dismally low in the financial year gone by leaving the miners fuming about their being left with mountains of pithead stocks was a foregone conclusion. As it would happen, Indian merchant exporters could not take advantage of the catastrophic rupture of Vale-owned tailings dam linked to a major iron ore mine in Brazil's Minas Gerais in January. The death of at least 230 people because of the accident forced the world's largest iron ore miner to pull 90 million tonnes (mt) of supplies. Irrespective of any commodity, such an occurrence would leave the market firmly in the grip of bulls.

TAKE TWO

Neither has there been a positive fallout on Indian exports from cyclone Veronica badly damaging its several iron ore export hubs in Western Australia in March. Indian miners are ruing that because of New Delhi not agreeing to drop export duty on ore with iron (fe) content of up to 62 per cent, for which the local demand is always poor, the country failed to take advantage of surges in global prices of the steelmaking ingredient to near five-year highs on production setback in the world's two largest production centres.

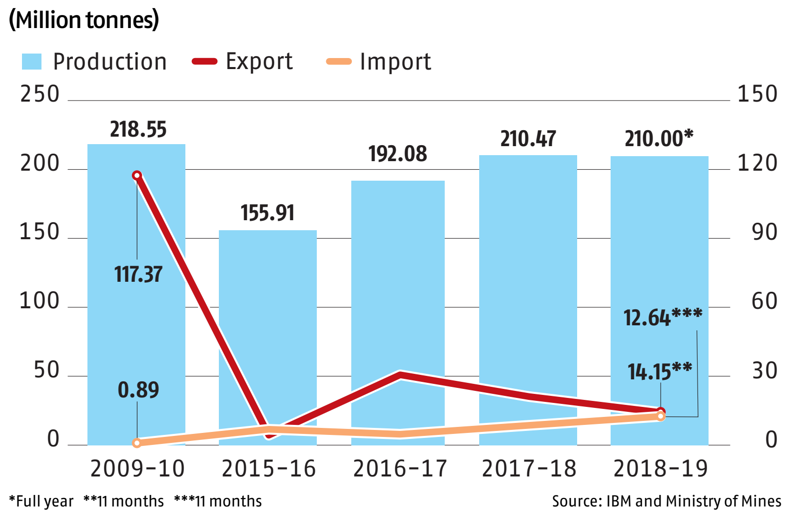
As dam rupture has curtailed Brazilian supply, cyclone affected BHP Billiton and Rio Tinto in turn have scaled down their production forecast for 2019. The certainty of shrinkages in the 1.5 billion tonne (bt) iron ore seaborne market has seen the price take a leap from $95 to over $100 a tonne, a development for the first time since 2011. But the material is still a long way off from the $187 a tonne seen in February 2011 when the price spike was triggered by supply disruptions in India. The previous peak of just above $208 a tonne happened in April 2008. But that price factored in a very high sea freight of $30 a tonne. The current Iron ore freight to Qingdao port in China from Australia is $6.43 a tonne and Brazil $16.3 a tonne.

Of greater relevance to India than where iron ore price will rule in the rest of the year is our virtual absence in the world market when bulls have everything going in their favour. It remains to be seen if the new government in Delhi will do away with the 30 per cent export duty on up to 62 per cent fe content ore to make the best of a global rally in the commodity and relieve merchant miners of accumulating pithead stocks. Analysts are in consensus that the seaborne market will tighten further through the rest of this year. London-based Liberum Capital says in a research report: "We have made significant upgrades to our iron ore price forecasts and now see risks prices could surge well through $110 a tonne in the second half of 2019."

An Odisha-based exporter says, Liberum changing its recommendation for BHP, Rio and Anglo American from "sell" to "buy" underpins the rally's strength. Vale has now given warning that another of its mining waste dams is at the risk of bursting. Even while the dam holds waste from a Brazilian mine inactive since 2016, it collapsing will add further strength to price rally.

MISMATCH

(Million tonnes)



*Full year **11 months ***11 months

Source: IBM and Ministry of Mines

A local industry official says: "Besides the production setback factor, the 4.5 per cent growth in world steel production at 444 mt in the first quarter of 2019, driven principally by China making nearly 10 per cent more at 231 mt, is fuelling iron ore price rises. China's GDP growth in 2019 may prove to be the slowest in 30 years. Surprisingly, however, iron ore on Dalian Commodities Exchange is drawing sustenance from some aggressive fall in Chinese port stocks." The point also not to be missed is shrinking inventory of steel rebar and hot rolled coils with Chinese mills creating condition for high production.

Shackled by high export tax, India could export only 14.15 mt in the first eleven months of 2018-19. While precise figures for the year are awaited, there was no extraordinary rise in shipments in March. In 2017-18 too, exports suffered a steep decline to 20.99 mt from 30.48 mt in the previous year. Not very long ago, India was the world's third largest exporter of the mineral. Exports peaked 117.37 mt in 2009-10 and then the combination of an adverse trade policy and court ordered restrictions on mining brought these down to 4.50 mt in 2015-16.

Take Karnataka where iron ore miners for the time being are reconciled to live with an annual production cap of 35 mt. But what they resent is that although they are not allowed to sell ore in other parts of the country, not to speak of shipments to foreign shores, steel mills close to coastal areas in the state are stepping up imports to keep local prices under pressure. Low import duty of 2.5 per cent is an incentive for Karnataka-based steel groups to use foreign origin ore in growing quantities. No wonder, then, India's iron ore imports in the first eleven months of 2018-19 climbed to 12.64 mt from 8.70 mt in 2017-18 full year.

There is a constant tussle between steelmakers and miners for the government's ear on export duty. Steelmakers want conservation of all iron ore, irrespective of quality for local value addition. Miners believe a country with a resource base of 33.276 bt, which is set to rise on intensive exploration, is well placed to meet growing requirements of local steelmakers and at the same time regain its status as a major exporter given the right trade policy. They say this is the only way to meet the steel industry's 2030-31 iron ore requirements of 437 mt to support metal production of 255 mt.

CHINESE WHISPERS

Queue of hopefuls

With access to the Prime Minister rather difficult since he had been travelling over the past few days, those hopeful of a ministerial berth have started approaching senior members of the erstwhile cabinet. Since Sushma Swaraj and Arun Jaitley are mostly not available to meet anyone, the hopefuls have crowded the residences of Rajnath Singh, Nitin Gadkari, JP Nadda and Thawar Chand Gehlot. By common consent, these former ministers are sure to get a cabinet post and are thought to be the ones who can get a word in with the Prime Minister or Bharatiya Janata Party President Amit Shah.

Will they, won't they

The Congress has won 52 seats in the new Lok Sabha. This means none of its leaders would be eligible for the Opposition leader status in the Lok Sabha. The status is granted to the house leader of the principal Opposition party but only if that party gets at least 10 per cent of the Lok Sabha's 543 seats. The Congress is a couple of seats short. A section in the Congress believes it is time that the Sharad Pawar-led Nationalist Congress Party (NCP) merged with the Congress. This, according to some, will serve two purposes. The NCP has five MPs in the new Lok Sabha. Merging with the Congress would take the Congress tally to 57 in the Lok Sabha, and would entitle the Congress party's leader in the House for leader of the Opposition status. Moreover, this could also help the two parties have greater synergy as they prepare for the Maharashtra Assembly polls in September-October. However, NCP sources have, until now, denied the possibility of a merger with the Congress.

Ducking after stepping out

The cricketer-turned-politician and the BJP's East Delhi winner, Gautam Gambhir (*pictured*), on Monday raised his voice on Twitter against the alleged assault on a Muslim man in the Gurugram neighbourhood. He asked authorities to take "exemplary" action in the matter. While Gambhir had invoked Prime Minister Narendra Modi's "*sabka saath, sabka vikas*" slogan in his tweet, not everyone in the Delhi unit of his party was happy with his public outburst. A section of Delhi BJP leaders were of the view that the party's newest member should focus on his constituency and urged him not to "interfere" in issues concerning Haryana.

ON THE JOB

Unemployment rate stabilises at 7%

MAHESH VYAS

The weekly unemployment rate bounced between 6.9 per cent and 7.7 per cent during May. The simple average of the rate in the past four weeks was 7.3 per cent. And, the 30-day moving average rate was 7 per cent as of May 26, 2019. With just five more days to go before the month closes, it seems likely that May 2019 would end with an unemployment rate of around 7 per cent, or a shade above 7 per cent.

With this, the monthly unemployment rate would have stabilised around 7 per cent over the past six months with a movement within a narrow range of 6.7 per cent and 7.4 per cent.

Last week, CMIE released its tenth Statistical Profile on Unemployment in India. This 200-page volume can be downloaded freely like all past volumes from *unemploymentinindia.cmie.com*.

CMIE completed the 16th Wave of its Consumer Pyramids Household Survey on April 30, 2019. This included the tenth Wave of its employment and unemployment surveys. The 16th CPHS field work was conducted from January 1 through April 30, 2019. The sample size was 174,405 households across the country and involved 715,273 members, of which 571,954 were of 15 years of age or more.

The survey did face execution challenges during this Wave because of the national elections. While the sample was the largest, the responses were slightly lower (by less than 2 per cent) than during the preceding two surveys. Nevertheless, the overall response rate was 84 per cent.

The Wave-wise estimates of employment/unemployment presented in the statistical profiles are the most reliable measures of labour statistics, particularly in comparison to the monthly, weekly or 30-day-moving daily estimates also released by CMIE.

During January-April 2019, there were 29.8 million unemployed people. A person is considered to be unemployed if s/he is willing to work and is actively looking for jobs but still cannot find a job.

Another 11.9 million were willing to work if work was available, although they were not actively looking for jobs. This is the potentially unemployed. If we add these to the 29.8 million unemployed, the greater unemployed stock works out to a substantial 41.7 million.

404.3 million persons were employed during January-April 2019. The labour force was thus 434.1 million (29.8 + 404.3) and the greater labour force was 445.9 million (29.8 + 11.9 + 404.3).

The unemployment rate works out to 6.87 per cent (29.8 / 434.1 X 100) and the greater unemployment rate works out to 9.35 per cent (41.7 / 445.9 X 100).

The biggest challenge that India faces is to harness these 42 million people who are willing to work independent of whether they are actively looking for a job or not. Their numbers are growing steadily. A year ago, they were 34.5 million during January-April 2018. Four months ago, they were 39.5 million.

The urban unemployment rate was higher, as usual, at 7.56 per cent during January-April 2019 in comparison to the rural, which was 6.55 per cent.

Male unemployment rate was 5.64 per cent while for women it was much higher at 15.77 per cent. This is line with our observations in our 9 preceding surveys on labour market conditions in India.

What is also in line is the finding that the labour participation rate of women is much lower at 11.02 per cent compared to the 71.54 per cent participation rate of men. Thus, once again, women face the double whammy of low participation rates and simultaneously, high unemployment rate.

Urban women are in a particularly poor spot. Only 9.8 per cent of urban women participated in the labour markets. This is lower than their rural counterparts who showed a greater participation rate of 11.6 per cent. But, urban women suffered a much higher unemployment rate of 20.8 per cent compared to rural women who faced an unemployment rate of 13.6 per cent.

Of the 404.3 million persons employed during January-April 2019, only 44.6 million were women. Of the 29.8 million persons who were unemployed in spite of being actively looking for jobs, 8.3 million were women. So, only 11 per cent of the employed population were women while 28 per cent of the unemployed were women.

Further, 60 per cent of the unemployed willing to work but not actively looking for jobs are women. There were 11.9 million persons who were unemployed and were willing to work but were not actively looking for jobs. Of these, 7.1 million were women.

This is not for the first time that the survey has shown the low labour participation of women in India. It may not be the last but, is there at least some change for the better? We will answer this question on another day.

The author is the MD & CEO of CMIE

LETTERS

Shallow pitch

Prime Minister Narendra Modi bowing reverentially before a copy of the Constitution placed in the Central Hall of the Parliament (*pictured*) brought back memories of his prostration at the steps of the Parliament on his maiden entry five years ago. For his addition of *sabka vishwas* (trust of all) to the catchphrase *sabka saath, sabka vikas* (solidarity with everyone, development for all) to be more than lip-service and have real effect, it must be more than a wish. Since Narendra Modi is a product of the *Sangh Parivar*, for which Hindutva is central to Indian nationhood, it cannot be said for sure that he would be able to practise what he preaches.

Ideally, Modi's life should be his message as it was in Mahatma Gandhi's case. We are sceptical about Modi's unity pitch because he once compared the victims of Gujarat pogrom to "puppies", referred to *shamshan-kabristan* in Uttar Pradesh and spoke of "majority-minority" demographic profile in Wayanad. The fact is that Modi owes his phenomenal rise in politics to his adherence to aggressive Hindu nationalism. His speech in favour of "inclusivity" or "inclusiveness" cannot carry much conviction for me. He must be speaking against the encroachment of religion into politics and not secularism. If there is indeed a change of heart for the PM on how to treat the minorities, we can gladly regard it as the best thing to happen to our country in which people of different faiths live cheek by jowl with each other.

Unless the homily on accommodating everyone is followed up with action, it won't achieve much or make any difference. Modi's claim that the election has broken down barriers and connected hearts is misleading. Actually, it has accentuated and reinforced religious distinctions (read fault lines). His statements that the minorities have been misguided and that the fear among them is only an illusion, require further elaboration. Nonetheless, there is nothing heroic about 80 per cent of the population demonstrating their might before a vulnerable lot.

G David Milton Maruthancode

Bold stance

This refers to the front page lead "Goyal, wife stopped from flying abroad" (May 26). One must laud the alertness of the immigration authorities for having acted on the look out circular in time. Calling back a "taxiing Emirates flight" must've needed some quick decision making and prompt bold action. I am sure such action against a very influential man would've required clearance from a high level. Whether Naresh Goyal is guilty or not, is for the investigating authorities and the courts to decide but it would've looked silly if the couple was out of the country when a decision eventually comes. Having yet another suspected fugitive sitting in London when he might be quizzed here, would've been a bad start for the new government. It would've looked politically incorrect. We all know too well how long, arduous and frustrating the extradition process can be.

Default debt of over ₹8,500 crore, obstinate refusal to step out of the C suite, grounded aircraft, 14,000 employees without any salaries and wages, CEO and many other senior executives having quit, multiple probes by different agencies and the Ministry of Corporate Affairs — these are reasons enough to prompt the staff union to approach the police and seek restrictions on Goyal and the senior management from leaving India. If indeed he is not guilty, he can very well stay in Mumbai and prove that to the investigators. Right from here, he can also engage in all possible meetings and measures to raise money for salvaging the airline. Perhaps Hindujas will prove the saviour in this situation and bring back this once India's finest airline its former glory. Good luck Mr Goyal.

Krishan Kalra Gurugram

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HAMBONE

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Bring back the Syndicate

Cong must dismantle 'high command', woo state satraps

After an election result that can only be described as disastrous, the president of the Congress party, Rahul Gandhi, reportedly informed the Congress Working Committee (CWC) that he would like to leave his post. What happens next is uncertain; the CWC, stocked with old-guard Congressmen who have risen to positions of power under the Gandhi family, supposedly rejected his resignation, but more recent reports suggest that Mr Gandhi himself is adamant about a change in leadership. Certainly, in most political parties around the world, a defeat of this magnitude would require a resignation at the top. But the Congress is not most political parties, and India is not most democracies. Even in other parties — from the Bahujan Samaj Party to the Akali Dal — it is hard to enforce accountability at the top for poor electoral performance. This is because it is frequently the leader or the first family that holds these parties together, in the absence of clear internal structures.

The question is how the Congress party might conceivably survive the possible exit of the Gandhis from a position of control (if not authority). There are some, such as psephologist-turned-politician Yogendra Yadav, who think that the Congress itself should die. That is, however, a somewhat extreme point of view, as the pole of national politics that the Congress occupies is valuable to the national discourse, even if the party itself has become moribund. The Congress itself has won only 52 seats in the Lok Sabha, insufficient even to lay claim to the position of leader of the Opposition. However, the larger Congress family needs to be taken into account. At joint fourth in the Lok Sabha, in terms of the number of seats won, with 22 each, is the YSR Congress from Andhra Pradesh and the Trinamool Congress of West Bengal Chief Minister Mamata Banerjee. The Nationalist Congress Party of Sharad Pawar won five seats and is already in coalition with the Congress in Maharashtra, which has second-highest number of Lok Sabha seats and where, however, the BJP swept the elections. Put these five members of the extended Congress family together, and it would have more than 100 seats in the Lok Sabha.

Any post-Gandhi party, which seeks to resurrect the original purpose of the Congress, must recognise the predominance of the states and the power of state leaders. One way to begin this process is by seeking to weld together the various Congress breakaway factions — which are after all together stronger today than the rump Congress led by the Gandhis. Both Mr Pawar and Jagan Reddy of the YSR Congress left the party thanks to differences over leadership positions with the Gandhis. It would be important thus for a post-Gandhi Congress to try and reverse those departures. Since the days of Indira Gandhi, the Congress has had a centralised "high command" structure. This has not helped the party in recent decades. It might be time to revisit the organisation that it had used till Indira Gandhi destroyed it — collective decision-making by a group of state-level satraps, known as the Syndicate. Vibrancy at the local or state level might then percolate up to the federal level and create a more potent opposition force to Narendra Modi than the Congress has been hitherto.

Second time lucky?

100% stake sale and lower debt can make Air India a better buy

The government has reportedly revived the plan to go in for a strategic sale of Air India and has asked the Air India management to finalise the financial accounts of the airline and its subsidiaries for 2018-19 by the end of June. A new expression of interest to invite bids is expected to be in the public domain within a month's time. This is encouraging news, because the sale of Air India has been hanging fire for a very long time and successive governments have failed to find a breakthrough. As a result, Air India has continued to be a drag on the taxpayers' account.

For instance, while its revenue went up from ₹20,526 crore to ₹22,146 crore between 2015-16 and 2017-18, net loss grew from ₹3,837 crore to ₹5,765 crore. The NDA government failed to clinch a deal for Air India in the last financial year as not a single entity showed any interest in picking up stake in the state carrier — perhaps with good reasons. The government, for example, offered just 74 per cent of its stake last year. This essentially scared prospective buyers who did not want to do business with the government as a partner. There were several other contentious provisions in the expression of interest that was released last financial year. For instance, the ₹5,000 crore net worth criterion for Indian carriers was simply a non-starter because only IndiGo met that condition. Carriers with zero or negative worth were allowed to participate provided they formed a consortium with other partners, together adding up to the stipulated threshold. But their stake was limited to 51 per cent of the combined 74 per cent shareholding in the airline, with the government holding the balance 26 per cent. This effectively meant that such Indian carriers could only hold 38 per cent in Air India. The terms also said the consortium shareholding pattern had to be frozen at the Expression of Interest stage and the winning bidder had to keep the Air India brand and operate it as a standalone airline on an arm's length basis.

Stung by the past experience, the government seems to be keen on ensuring that those mistakes are not repeated. For example, instead of 76 per cent stake sale, this time around the government wants to let go of 95 per cent stake, keeping aside just 5 per cent for the purpose of providing for employee stock options. Another big stumbling block last time was the level of debt on Air India's books. Here too, the government seems determined to make amends — it has already decided to transfer ₹29,464 crore of Air India's working-capital debt not secured by an asset to a new company, which the government hopes to pay back by monetising some of the airline's profitable subsidiaries. This leaves the airline with a debt of ₹25,000 crore, mostly long-term debt secured by aircraft purchases. This means the interest outgo will come down substantially to around ₹1,700 crore a year. This is within manageable limits for an airline which will reign supreme in the vast US and North American markets after the closure of Jet Airways. Since more than half the 163 aircraft are owned by Air India, the new owner can monetise them and lease them back. The resounding win at the Lok Sabha elections has presented an opportunity for the government to walk the talk.

An action plan to energise defence

Here are some points for the new govt to consider in redressing the systemic weaknesses in defence


BROADSWORD
AJAI SHUKLA

The perception that the outgoing National Democratic Alliance (NDA) government was strong on defence and security was a significant factor in its re-election. In truth, whether in defence allocations, procurement reform, restructuring higher defence management or creating an indigenous defence industry, the NDA only followed in the indifferent footsteps of the United Progressive Alliance government before it. Yet, the NDA generated the impression of strength by actions like the cross-border "surgical strikes" of 2016, the Doklam standoff against China in 2017, the February air strikes on a terrorist camp at Balakot in Pakistan and by talking tough on Pakistan and Jammu & Kashmir. The incoming government knows that, had any of this led to a serious military escalation, systemic defence weaknesses could have been exposed. Therefore, to redress shortcomings, here are three suggested action points in defence philosophy, three steps for the medium-term, and three immediate measures for South Block's 100-day agenda.

Changes in philosophy

First, the government must establish a clear threshold for defence capital allocations, which cater for equipment modernisation. Raising capital allocations is not difficult, even given political compulsions for spending on development and populist schemes. With the existing defence allocations already providing fully for revenue spending, any spending rise would go straight into the capital head, creating an out-of-proportion impact. For example, an in-principle decision to devote 30 per cent of the defence budget to capital procurement (against the current, inadequate 25 per cent) would require a ₹30,000-crore rise in capital allocations over the interim Budget of February. Even with this rise, defence allocations would remain at 16.5 per cent of total government spending, unchanged from 2018-19; and at a modest 2.2 per cent of the Gross Domestic Product.

Second, while every government has paid lip service to defence indigenisation, none have thought hard about how to encourage it or what route to take towards building Indian weaponry. Given the technological inferiority complex that plagues our defence ministry and military, they have unwisely plumped for the "strategic partner" (SP) route, in which Indian firms build foreign weaponry based on transfer of technology (ToT) from foreign vendors. In fact, little technology of value is transferred, only "manufacturing ToT" and blueprints, but not the capability to design, modify and upgrade weaponry. For that, India must develop systems engineering processes and capabilities, which is achievable through the "Make" route, not the SP route. The latter's ToT-based manufacture creates dependencies on the foreign vendor that last through the platform's service lifetime. In contrast, engineering a platform ground-up gives us not just a weapon and the wherewithal to maintain it, but also the design skills, experience and infrastructure needed to evolve that into subsequent generations.

The Defence R&D Organisation (DRDO) has illustrated the benefits of ground-up systems integration in its strategic missiles programme. Its liquid-fuel Prithvi and solid-fuel Agni missiles were incrementally improved into more accurate, longer range, canister-launched missiles like the Agni-IV and V. This accumulated expertise then led to the development of an anti-ballistic missile shield, and those technologies fed into the anti-satellite test in March.

Similarly, the DRDO's Akash anti-aircraft missile and Pinaka rocket launcher are being incrementally improved into more lethal and accurate weapons. The Advanced Towed Artillery Gun Systems (ATAGS), which the DRDO is developing in partnership with Kalyani Group and the Tatas, will wean us off buying artillery guns from abroad, since the ATAGS design expertise will constitute the foundation for building future artillery guns. Similarly, the Tejas will create an indigenous ecosystem for building the advanced medium combat aircraft. Hence the government must strongly push indigenously designed and developed platforms, permitting SP projects only as interim solutions to bridge capability gaps until an indigenously designed solution is evolved.

Third, to create the ecosystems for indigenous design, development and manufacture, the defence ministry must unapologetically function as a market maker, given that the weapons bazaar is a distorted market characterised by both monopoly (single seller) and monopsony (single buyer). For most weapons, India's military can support just one domestic source of supply, especially without the backing of large export orders. Even so, the defence ministry must select and develop a private sector rival to each of the eight defence public sector undertakings, while also exposing the ordnance factories to open competition. With no place for two private firms in each weapons area, hard choices must be made. As part of its market maker role, the defence ministry must also create regulatory frameworks, testing infrastructure, certification agencies and a more credible version of the Technology Perspective and Capability Roadmap that was first put out in 2018 — but lacks credibility within industry. A positive first step was the government's acceptance last week of self-certification by established defence manufacturers.

Medium-term steps

First and the most essential, make Indian defence industry competitive vis-à-vis foreign competitors and the public sector by reducing the cost of capital. Given inflation and interest rates, Indian firms pay 8-10 per cent more each year than their foreign competitors, severely impacting costs over a product gestation period of 7-15 years. Incentives must also be extended for research and development, which Indian industry enjoyed under Section 35 (2)(a)(b) of the Income Tax Act, but which ends in 2020 under a sunset clause. Finally, defence infrastructure, such as testing and certification facilities, must be granted infrastructure status under Section 80L. Even hotels enjoy infrastructure benefits, but defence and aerospace are ineligible.

Second, a raft of policies initiated under the previous government, such as the Defence Production Policy, need to be finalised and implemented. The idea of Innovations for Defence Excellence, which aimed to encourage innovation amongst small firms and individuals, has failed to link up with actual procurement. Similarly, the Technology Development Fund has resulted in no assurance of orders. Direct linkages must be ensured between development, production and procurement.

Thirdly, the government must kick-start the development of information technology-based technologies, which are a natural area of excellence given India's software skills. An immediate investment of ₹3,000-₹4,000 crore must go into developing cyber technologies, artificial intelligence and ISTAR (intelligence, surveillance, target acquisition and reconnaissance) technology — a huge force multiplier that manages battlefield sensors and the information they gather.

The 100-day programme

Immediately, release procurement orders languishing in the pipeline for indigenous defence platforms that are essentially improved versions of platforms already in service — including the Akash, Pinaka, strategic missiles, Tejas Mark 1A.

Sanction a mission mode project to create an indigenous data link to connect all three services' drones, fighter aircraft, warships and land combat vehicles. This crucial command and control software should be overseen by a body that incorporates DRDO, the Indian Space Research Organisation, Council for Scientific and Industrial Research, academia and private industry. In coordination with the foreign ministry and relevant countries, release funding and sanction for defence exports to regional partner countries, such as offshore patrol vessels for Indian Ocean island states, helicopters for small neighbours, etc. Besides their value in defence diplomacy, this would galvanise defence industry.

PROPOSED CAPITAL ALLOCATION RISE
(₹crore)

	2018-19 (RE)	2019-20 (Interim)	2019-20 (Projected final)
Revenue budget (including pensions)	3,06,720	3,22,878	3,22,878
Capital allocation	98,473	1,08,133	1,38,133
Total defence budget	4,05,193	4,31,011	4,61,011
Capital allocation as %age of total defence budget (%)	25	25	30
Central government spending	24,57,235	27,84,200	27,84,200
%age of govt spending (%)	16.50	15.50	16.50
Gross domestic product	188,40,731	210,07,439	210,07,439
Percentage of GDP (%)	2.15	2.05	2.20

Source: budget documents

Corporate governance of PSUs: A case for change


UK SINHA & SAPARYA SOOD

Post-independence, the need for rapid economic development, coupled with lack of financial, technological and managerial strength in the private sector, led to a policy for promoting Public Sector Undertakings (PSUs). Laws were enacted to provide them with special protection and privileges. However, their provisions have, by and large, remained static and led to dilution of corporate governance principles. There is relative lack of accountability and transparency compared to the mandate for companies in the private sector. Now, there is a strong case for similar laws and regulatory treatment for all companies — irrespective of whether the majority owner is the government or a set of entrepreneurs from the public.

Differential treatment is meted out to PSUs through the following mechanism:

1. Specific provisions in laws passed by Parliament or the rules/guidelines issued by the government under these laws.

2. Special provisions in the regulations framed by regulators or the case by case exemptions routinely granted to PSUs.

3. Condoning or soft-pedalling PSU violations by giving them a special treatment.

We will deal with each of them now. Section 462 of the Companies Act, 2013 (Companies Act) allows the government to exempt certain classes of companies from the application of any provision of the Act in public interest. The provision has been liberally used to grant exemptions to PSUs.

Directors of a company are disqualified if the company has failed to repay the depositors, or redeem debentures or interest on the due date or if it has not filed its annual returns or financial reports for a continuous period of three years, but directors of PSUs are exempt from this. The board of a company has a role in the appointment of directors or in their evaluation. But not so for PSUs. It is done by the administrative ministry. PSUs are exempted from disclosing their policy on appointment and remuneration of directors and also the criteria laid down for determining qualification, positive attributes and independence of an independent director. No wonder, then, that in successive governments, office bearers of the party in power end up cornering board positions in PSUs.

The general rule that a person should not be allowed to take loans from the company where he is a director, again, has an exemption for PSUs where it is possible to do so with the approval of the administrative ministry. Powers of the board or its committees such as the audit committee, nomination and remuneration committee which are exercised by a company are vastly suppressed in areas like appointment of auditors in case of PSUs where their powers are vested with the government.

Independent directors perform a very important function in the current scheme of law. One of the criteria for independence is that independent directors should not have any pecuniary relationship with the company or its associates. However, strangely, this requirement is not applicable to PSUs. The process of appointment of independent directors on the boards of PSUs is another area of improvement that needs to be looked into. Currently, there is an elaborate multi-stage process in the government requiring the approval at the highest level. But this is not in consonance with the philosophy that an independent director is not the nominee of the majority shareholder.

One important tool to prevent manipulation in share prices of listed companies is to have a minimum public shareholding (MPS) in these. Rules framed by the government under the Securities Contract (Regulation) Act prescribe MPS at 25 per cent. But the earlier level prescribed was only 10 per cent for PSUs. Reluctantly, when it was enhanced to 25 per cent in 2014, three years' timeline was given for compliance. Later, it was extended by a year in 2017 and by another two years in 2018. There are reports suggesting that the timelines for public sector banks are likely to be extended beyond 2020. On the one hand the rule is framed by the government using powers under law; on the other hand, government as the majority owner is the sole beneficiary jeopardising the interest of ordinary shareholders of these PSUs.

Another example is the corporate governance guidelines issued by the government in 2010 (DPE Guidelines). There are huge gaps between these guidelines and the provisions under the Companies Act and SEBI LODR Regulations. But these guidelines have not been revised and the anomalies continue.

It is not our case that the hands of the government remain fettered even if there is a situation of public interest being seriously jeopardised or in matters of national security. In such exceptional situations, there may be a case for providing exemptions. But, unfortunately these are being adopted and used in a routine manner.

In part II of this article, we will talk about the other two mechanisms, namely (i) specific exemptions in regulations framed by regulators and, (ii) condoning violations by SOEs. We will also evaluate the implication of these provisions and exemptions.

The second and concluding part of this article will appear tomorrow. Sinha is senior advisor and Sood is an associate with Cyril Amarchand Mangaldas

Salty nuts of Empire


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Even though collectively the English are amongst the nastiest people in the world, they do produce some quite endearing individuals if only for their nuttiness. I discovered one such last month.

Indeed, think it might be a good idea for someone like Ram Guha to write a book called *The English Nuts of India*. The Brits will love it because they make such a point about being eccentric.

The guy I discovered is called Roy Moxham. Back in 2002, he wrote a book back about how, in the latter part of the 19th century the bandits who ruled India built a 2,300-mile long hedge. The idea was to prevent the smuggling of salt between British India and the Indian states.

The hedge, yes hedge, was 20 feet deep in some places and about that high as well. The book is called, rightly, *The Great Hedge of India*.

One day in 1994, Moxham discovered this long forgotten nugget by accident. Piqued at how anyone could have thought this up, he decided to see if any of it was still left.

So he turned up in India in 1996 and kept coming back until he found it five years later somewhere in Uttar Pradesh. He has described his adventures in this book, including an incident when a crocodile turned up when he was taking a dump on the banks of a river.

Salt taxes started during Chandragupta Maurya's time. The thing is, says Moxham, no one protested until the avaricious criminals of the East India Company raised the rate a hundred-fold

The book also contains a detailed account of the history of salt taxes in India. They started during Chandragupta Maurya's time. The thing is, says Moxham, no one protested until the avaricious criminals of the East India Company — have no doubts, that's what they were — raised the rate a hundred-fold. And because they were pocketing the proceeds — a few billion pounds over 100 years from 1760 — the British government, which took over British India in 1860, decided to build the hedge.

The other reason for building the hedge was that because salt taxes in British India were so high, people started smuggling it across from the Indian states. Since there was no money to build a wall, the customs department — corrupt as ever — decided to build the hedge with watch towers and little forts along its length. Their remnants is what Moxham found.

This crazy idea lasted for just a decade from 1879 to 1890 when it was abandoned. The man who made it truly affective was none other than the founder of the Congress party — Allan Octavian Hume. At its peak it wound its way from Multan all the way to Bihar. It is amazing that some villagers in UP remembered when Moxham met them 120 years later. They said it was known as *parmat lane* (permit line).

Self-serving nuttiness

English nuttiness, although portrayed as their eccentricity now, was never without a self-serving purpose. For example, the circuit houses and the dak bungalows they built in remote places all over India had a hidden purpose as well — the good old binkitty-bonk on the side.

There were many delectable and salacious stories about the love life of the *sahibs* who would bring along their girlfriends for an amorous week or so while the *memsahib* was away in England. They remain a place for comfortable liaisons between male and female officers who were attracted to each other.

These circuit houses and sometimes even the dak bungalows were exclusive and highly subsidised micro-sized hotels built in picturesque locations where the white officials of the Raj stayed while on tour. They were as essential to governing India as the police and army were because the Raj was run on the hoof.

The circuit houses were for the higher ranks and the dak bungalows for the lower ones in the middle of dense forests.

Many had now forgotten ghost stories attached to them. The dak bungalow at a place called Misrodh near Bhopal had the story of one Miss Rod — Misrodh, get it? — who committed suicide after her heart was broken by some cad of an Englishman.

Then there is the story of a circuit house near Jabalpur. An Englishman's ghost would visit there over Christmas. He had killed himself out of sheer loneliness. There were many like him.

Much of all this was captured in a book on these Raj babu resorts by Rajita Bhargava a few years ago. Like Moxham with the hedge, she decided to find out what these things were and have become. Unfortunately, the book is out of print and I can't remember its name.