

# Opinion

THURSDAY, MAY 9, 2019

## VOTE FOR WORK

Union minister and BJP leader Maneka Gandhi

When we work, we work for all and that time nobody is concerned about Lotus, but when it is time to vote and people tell us that they will not vote for me because they don't want to vote for the lotus symbol, it feels very bad



## REFORM REQUIREMENT

FROM PRIVATISATION TO FORCING STATE-RUN POWER ENTITIES TO REDUCE LOSSES, THE INCOMING GOVT MAY HAVE TO BITE THE BULLET ON SEVERAL KEY REFORMS

# A difficult time awaits the next government

**A NEW GOVERNMENT WILL** be formed by the end of this month. The current political occupation of minds will soon end and attention will turn to the economy. The arriving government will have to confront several problems—some longstanding, others more recent. While the departing government introduced some key reforms, especially the IBC and a nationwide GST, it has to be said that it also ducked or shied away from taking several other important reforms—dubbed as ‘hard’ options in political economy context. In some cases, it also avoided even softer options. The overall picture is of serious impediments in some segments that require urgent reform or resolution if encouraging private investment is a policy priority. The pretext of ‘all is well’ will have to be shed as these can no longer be brushed under the carpet. Undoubtedly, the new government will be challenged in redressing these because of a significantly weakened fiscal position, decelerating growth and an uncertain outlook.

The topmost concern is the vulnerable financial system. Both public and private banks are beset with unique issues. Those in the public sector banks are old—monumental overhang of bad assets leading to a virtual retreat from crucial functions such as lending and transmission of monetary policy actions. The main casualty of this stalemate has been the economy. The NPA problem was initially allowed to fester by the outgoing government with modified restructuring schemes, a lightweight reform package (Indradhanush) and the failed gamble of growth-driven resolution. Recognition and disclosures did accelerate thereafter, but insufficient recapitalisation and slow-paced resolution have prolonged the impasse. The most glaring omission in this regard is the departing government shied from taking hard decisions such as privatisation, and even the easier option of governance reforms to professionalise functioning if it preferred retaining public ownership.

The pending public banking reforms will now be the next government's charge. Should it take the ‘hard’ privatisation route? Or should it take the ‘soft’ course of governance overhaul recommended by the Nayak Commit-

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tee? These are the choices it faces. Then again, governance and disclosure issues have surfaced in private sector banks too in last two years. Will stronger supervision, sterner regulatory actions suffice to avoid repetitions? Or is it time to debate reform of private banks' governance structures equally?

In the last one year, the banking system's vulnerabilities spread to the non-banking segment, which grew rapidly to fill the lending vacuum. The IL&FS default last October exposed serious faultlines, including that of regulation, in the NBFC segment and related financial market parts. Default risks and costs have since remained elevated with occasional eruptions, downgrades and gathering expectations of a vicious, market-driven elimination of ‘lemons’ and survival of the fittest. Tighter regulation to address asset-liability mismatches in NBFCs is in the pipeline. But the next government needs to consider the speed of consolidation likely to occur here as NBFCs are a vital financing source for those unable to access banks. Again, there is the ‘soft’ option of handholding, protection to unviable, weak entities or the ‘hard’ choice of letting these fail.

Next is the nonfinancial corporate sector where defaults and failures have risen. Aviation and telecom are two struggling segments. The leaving government did try selling the ailing public airline, but was unsuccessful. Meanwhile, a large private airline, whose precarious condition was inordinately stretched but eventually went bust last month, has tossed aviation into a mess. The arriving government will have to choose between the hard choice of renewed sale of the public airline and the ‘soft’ option of turning it around, in which case it must scramble enough resources to put it back on track. It will also have to accelerate resolution of the failed private airline to restore civil aviation health.

Similarly, the retiring government dragged its feet over the ‘hard’ option of divesting two public telecom firms, BSNL and MTNL. The new government will have to bite the bullet on these, i.e., choose tough action and sell these off for a leaner, healthier telecom sector. Indeed, there is no soft option here!

The power sector comes up next. The much-touted UDAY scheme to reform the power sector has failed to improve efficiency and viability; it was always an old idea that had been tried and failed but was presented as new. A huge amount of capital lies locked up in 30-odd debt-laden firms (combined debt estimated above ₹1.5 trillion) with 39,000 MW of production capacity. The retiring government dithered on this too, i.e. shying away from tough action to force reform at state-owned entities to reduce losses and raise revenues, nor fully resolving issues surrounding fuel-availability, power-purchase agreements, and promoters' inability to infuse equity/working capital, etc., while risk-averseness of banks/financial institutions magnified the problem. The next government will have to weigh the ‘hard’ and ‘soft’ choices urgently. It is bad enough this capital remains unproductive, but will be worse if eventually liquidated for the scale of capital destruction would be an adverse portent for future investments.

There is also the rest of infrastructure sector, where stalled projects remain accumulated and private participation is restricted to EPC projects. This testifies to risk-aversion that persisted throughout the outgoing government's tenure. There is also the ‘unease’ of doing busi-

ness and ‘fear’ of tax-terrorism. The next government will have to improve this environment.

The departing government also conducted questionable divestments such as takeover of one PSU by another to merely drawdown cash for fiscal targets. For example, ONGC bought HPCL, PFC bought out REC, stake sale of NHPC to NTPC, and so on. These ingenuities squeezed out almost all surplus cash lying with PSUs, leaving little retained earnings for their investment and profitability, e.g. ONGC's cash reserves plunged to ₹167 crore in Sept. 2018 from ₹9,511 crore in March 2017 after HPCL acquisition, hefty dividend payouts, etc. The new government must

work on a genuine divestment policy, similar to one followed by NDA-1. Given the budgetary constraints, this is a must—there is no other option.

The many hard decisions avoided by the departing government fall into the incoming one's lap amidst a worsened fiscal position. On the macroeconomic front, the overarching, fundamental question is of high real interest rates. While the retiring government controlled inflation, the real rate did not decline. How to bring down the real cost of capital is the

important question for the next government? Monetary policy is committed to price stability; it can accommodate growth only within the inflation target bounds. That leaves the ‘hard’ option of greater fiscal compression than the current consolidation roadmap. The outgoing government also avoided ‘hard’ consolidation, e.g., subsidy reduction, primarily food subsidy, expenditure on which ballooned; it chose instead the easier path of direct benefit transfers. The new government will now have to seriously consider expenditure rationalisation at a time when tax revenues have slowed, non-tax revenues have nearly emptied out. A lot on the plate out there for the next government to worry about once the victory euphoria subsides.

## Is the MCA-21 a black box that is distorting GDP data?

CSO must explain how the presence of shell companies doesn't inflate GDP & how it verifies the information put out by firms

**DOES THE PRESENCE** of a very large number of shell companies in the MCA-21 database—maintained by the Ministry of Corporate Affairs (MCA)—that is used for calculating GDP in the country negate these numbers? According to a report in *Mint*, the National Sample Survey Office's “Technical Report on Services Sector Enterprises in India” found that around a third of the number of units in the MCA-21 database that were being canvassed for another survey could either not be traced or they were wrongly classified. Does that mean the manufacturing/services data that is based on the MCA-21 series is exaggerating the GDP in a big way? Former National Statistical Commission chief Pronab Sen—he was also the first Chief Statistician of India—told *Bloomberg Quint* that just because there were a large number of shell companies, it didn't necessarily mean the GDP was exaggerated as the shell firms were being used by other firms who were producing something but wanted to hide it from the tax authorities; to that extent, Sen argues, removing the data of these shell companies will understate GDP.

It is not clear if the explanation is *kosher* as no one knows whether the fake bills being generated are equal to or greater than the amount of genuine sales—from service or manufacturing firms—but even when the statistical authorities were debating whether or not to use MCA-21, there were some misgivings. A sub-committee under Professor B Goldar looked into the matter and while it found that the GVA estimates for manufacturing were 29% higher using MCA data as compared to the traditional method using RBI data for FY12—and 34% for FY13—it added a caveat while recommending MCA-21 be used instead of RBI's sample that was blown up to represent all companies. The sub-committee did a check on the MCA data for 500 companies that gave data using XBRL—extensible business reporting language—and found that this tallied with their annual reports in most cases. However, it found, that “for unlisted companies no alternative information is available in public domain... Hence any kind of validation exercise is not feasible there”. It concluded by saying “it is strongly recommended that MCA should evolve a system for data validation to ensure the accuracy of online data reporting through MCA 21”.

Whether a reasonable validation regimen has been put in place is not clear, but as economist Renu Kohli pointed out in this newspaper, it is odd that the ‘periphery’—the majority of the unlisted firms in the MCA-21 database—should so consistently outperform the ‘core’; for FY18, RBI's sample of 3,000-odd listed non-government-non-finance companies saw a 5.2% increase in ebit while the GVA for manufacturing (from GDP data) grew by 12.4%, by 13.9% for construction, 11.8% for trade, etc. The larger changes in data every year based on this data are equally worrying—manufacturing GVA for FY16 was estimated to have grown at 9.6% when the estimates were released in January 2017, but this rose to 12.7% when estimates for the same year were made in January 2018 and to 14.3% in January 2019. In which case, how is one to believe the data? At the very least, those in charge of data-gathering in the government need to come up with a reasonable explanation for this to resolve the apparent contradictions. Of course, the flipside of this is that, were this to be done for the use of MCA-21 data, a similar explanation will need to be given for the jobs data, for the GDP back series, etc.

## Transparency vs state secret

“Public interest” remains a powerful touchstone for OSA

**THE CENTRE'S CONTENTION** that the Supreme Court waiving the penal provisions against publication of information protected by the Official Secrets Act (OSA) threatens the integrity of the Indian state is an overstatement of the likely impact of the apex court's order allowing use of leaked Rafale documents in a plea seeking the review of the defence deal. The Centre's stand is portentous since indiscriminate application of OSA can have a chilling effect on the freedom of the press and whistleblowing by public officials and employees of concessionaires in government contracts. Had the OSA been invoked and been considered binding at the time, a 2G or a coal scam could never have been exposed. Allocation of public resources would have probably remained as graft-prone today as then. The government's stand in keeping with the amendments that it wants made to the Whistle Blowers Protection Act that have been stalled in the Rajya Sabha since 2015. The amendment Bill not only revokes the immunity granted to whistleblowers from prosecution under the OSA, but also makes whistleblowing impossible. The law, from centring on protecting information relating to only national security from disclosure, would cover trade secrets, foreign relations, fiduciary relationships, etc—all of these being criteria that would offer protection to Rafale-related documents—if the amendment Bill gets passed. It also debars the disclosure of information obtained by any other means than RTI, and requires the clearance from authorities who may themselves be implicated if the documents are made public. Such a deliberately expansive view of what constitutes official secrets is surely not *kosher*?

The SC bench offered sage legal rationale in allowing the leaked Rafale documents. The three-judge bench maintained that there is no provision in the OSA or any other statute under which Parliament empowers the executive to “restrain publication of documents marked as secret or from placing such documents before a court of law which may have been called upon to adjudicate a legal issue”. The Chief Justice of India, Justice Ranjan Gogoi, used the apt example of the US Supreme Court's judicial wisdom in refusing to recognise the executive government's right to restrain the publication of the Pentagon Papers that detailed the abject failure of the US's Vietnam strategy. The Centre, in its affidavit presented at the SC, claims that this could make all closely guarded secrets “relating to space, nuclear installations, strategic defence capabilities...” vulnerable. What this bogey-man argument misses completely is the “public interest” touchstone of whistle-blowing. Indeed, the whistleblower or a news organisation collaborating with the former is hardly likely ignore the legal implications if the matter being leaked doesn't stand the test of “public interest”. The SC also cited Section 8(2) of the Right to Information Act to say “notwithstanding anything in the Official Secrets Act and the exemptions permissible under sub-section (1) of Section 8, a public authority would be justified in allowing access to information, if on proper balancing, public interest in disclosure outweighs the harm sought to be protected.” This forceful vote for transparency is far more preferable to intransigent opacity in the name of state secrets.

## TrustVOTE

SC rejects the demand for 50% VVPAT verification; EVMs may have flaws but paper ballots allow easier subversion of democracy

**COME POLL SEASON**, and some parties that foresee their loss raise the EVM-tampering bogey. Given how the allegations, if they aren't probed, could erode the trust of the electorate in India's democracy, the Supreme Court did well to allow voter-verified paper audit trail (VVPAT) verification at five polling booths per assembly segment, instead of just one booth per assembly segment as was the norm earlier. One booth per assembly segment translates into less than 1% of the total polling booths in the country, thus, it makes it difficult to catch any tampering if it was happening, opposition parties that has petitioned the Supreme Court in the matter had contended. However, by rejecting the demand of 21 opposition parties that 50% of VVPAT be verified, the SC court has done justice to the electorate as well as the democratic process in India.

A 50% verification would mean that the Lok Sabha counting will get delayed by six days, a delay that the petitioners are okay with. However, given how they haven't been so far able to prove that EVMs can be hacked, opposition parties drumming up bogey-man fears is a serious disservice to India's democracy. While the Aam Aadmi Party demonstrated the hacking of a non-ECI EVM in the Delhi Assembly, none of the political parties that have been stoking EVM-scepticism actually took of the ECI's open challenge to hack its machine. On the other hand, the ballot system, as the panchayat elections in West Bengal last year showed, allows for far easier booth-capturing and casting of bogus votes. Are those the days that the opposition parties want to drag the nation back to? If so, doesn't this mean that the parties claiming that democracy is being subverted would be the actual beneficiaries if indeed democracy is subverted with paper ballots?

## Facebook is its own worst political enemy

Zuckerberg's and Clegg's attempt to please EU lawmakers is falling flat. The need for more regulation of the company hasn't gone away

**LIONEL LAURENT**

Bloomberg



**THE FORTHCOMING EUROPEAN** parliamentary election was meant to be Facebook Inc's big chance to please a constituency that trashes it on a regular basis: Politicians.

After all of the controversy around fake news on the website and the Cambridge Analytica scandal (where Facebook user data was harvested for political purposes), the company hired the former British Deputy Prime Minister Nick Clegg to help clean up its act. The social network has announced a slew of measures intended to fight misleading news stories and foreign meddling in elections, including: Tougher oversight of political ads, a fact-checking operation, and more content moderators to block abusive content.

Clegg was meant to be a dream hire as Facebook's global head of public affairs because of his insider knowledge of Brussels, where he worked as an official for years. The European Union has been especially forthright in wanting to crack down on Facebook. Yet the company's new measures have already fallen flat with just weeks to go before the European vote. In fairness, some of this may just be clumsiness, but it's a poor start to Clegg's campaign to win around the policymakers.

The company's new transparency drive to combat foreign interference, for instance—which requires advertisers to register in each specific member state where they want their content to appear—is a problem for mainstream pan-EU campaigns that are a feature of these types of elections. The result has been a backroom spat between Clegg and EU officials over whether exemptions can be

granted.

Worse, it's not even clear that Facebook has the ability to enforce its own rules. Several news organizations have shown how easy it is to get approval from the social network for political ads with false information. Even when trawling the website's European “ad library”—a searchable database of ads intended to promote transparency—you still see troubling examples. One ad in France that praised far-right leader Marine Le Pen's top European candidate was pulled for not complying with Facebook disclosure rules, but not before getting thousands of impressions.

Hiring more foot soldiers is one way to stop the spread of fake news designed to polarize opinion and generate outrage, but it's a monumental task to catch everything and their army of content moderators is still not big enough. Data firm Alto Analytics recently tracked the spread of a Dec.

2018 story from Infowars, the site run by conspiracy theorist Alex Jones, which claimed several French generals had accused Emmanuel Macron of “treason” over last year's United Nations migration pact (it failed to mention the generals were retired and had links to the far right). The piece was picked up by several media brands, and Alto found that 1,828 users shared Russia Today's version.

Facebook CEO Mark Zuckerberg says there's no way to guarantee an “interference-free” election, and that the challenge is an “ongoing arms race” against sophisticated actors. But the problem for Facebook is that its own weapons have a habit of ending up in the wrong hands. This is a network whose business model of targeted advertising depends on intimately knowing users' habits. And these data have been exploited in disturbing ways, from the hoovering up of personal information by Russian operatives to influence the 2016 U.S. presidential election to housing discrimination. Facebook's tweaks to its model have come in fits and starts, and after the fact.

All of which means the company will remain a target for EU politicians. Guy Verhofstadt, leader of the European Parliament's liberal grouping, called last week for more regulation of Facebook and even suggested building a state-funded alternative to the social network. That latter idea is clearly far-fetched, but there's still a real need for a robust policy response to the market power, political toxicity and failed self-governance of Facebook and other social networks. Clegg can't work around that.

**Facebook CEO Mark Zuckerberg says there's no way to guarantee an “interference-free” election, and that the challenge is an “ongoing arms race” against sophisticated actors. But the problem for Facebook is that its own weapons have a habit of ending up in the wrong hands**

## LETTERS TO THE EDITOR

### India headed towards a coalition govt

Most people have not become fatigued or lost interest in politics despite the long-phased polling and the long wait for the election results. Now the conversation, be it at home, workplace, tea stalls or elsewhere centres on who will become the next Prime Minister. While the results cannot be predicted with any certainty, it appears that no party or alliance is going get a majority on its own. A hung Parliament appears to be what we are headed to. One thing is for sure—it is going to be a coalition government. The parties that are inclined to be part of a coalition government led by Congress outnumber the parties that feel at ease in BJP's company. The Opposition is so optimistic that it is reported to have decided to knock on the President's door soon after the announcement of the results to stake claim to form the next government and pre-empt any kind of manipulation by BJP. The key to government formation will be certainly in the hands of regional parties. It is unlikely that the BJP will make up for the losses in states where it reached the saturation point in 2014 with the gains it now hopes to make in states like West Bengal and Odisha. If BJP manages to cross, say the 220 mark (unlikely), it will seek to cobble up a government with parties that are ideologically not very hostile to it. No assurance might persuade the DMK to join hands with BJP, given its passionate opposition to what the saffron party represents. If the Congress crosses, say the 140 mark (likely), it could attract the major regional parties to be part of a government led by it.

— G David Milton, Maruthancode

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PORTRAIT: SHYAM KUMAR PRASAD

● **RECORD CAFE: ARGHYA SENGUPTA, CO-FOUNDER, VIDHI CENTRE FOR LEGAL POLICY**

## In the dock: Judicial accountability

*It is almost an article of faith in India that, to preserve judicial independence, the judiciary mustn't be made to submit to any kind of accountability other than what it alone proffers. The fear of judicial independence getting eroded holds so firm that it has helped the judiciary tide over what- ever crises of faith the masses may have had. Arghya Sengupta of Vidhi Centre for Legal Policy examines the contrived independence/accountability binary in the context of the higher judiciary in his book 'Independence and Accountability of the Indian Higher Judiciary' since the higher judiciary frames the rules of judicial governance in India. In an e-mail interview, Sengupta tells Sarthak Ray, among other things, why the current controversy over alleged sexual misconduct by the Chief Justice of India (CJI) has links to how the higher judiciary has interpreted judicial accountability over the years. Excerpts:*

The way the Supreme Court has handled the allegations of sexual harassment—by a former employee against the CJI—has brought the top court and, indeed, the higher judiciary under a cloud. Where is this problem rooted? Does it relate to the overall lack of accountability of higher judiciary?

I don't think the proceedings of the in-house committee inquiring into allegations of sexual harassment against the CJI can, and should, be seen in isolation. Their method of functioning is a direct product of the in-house procedure to inquire into judicial indiscipline. This procedure itself is based on a simplistic view that judges alone can be trusted to deal with matters relating to fellow judges. This trusts not only to discipline, but to transfers and appointments as well. The conceptual cover for this view is provided by judicial independence. However, as I argue in my book, judicial independence has today become a sword to be wielded at will rather than a shield against excessive governmental interference. Judges cannot simply state that any demand for transparency such as disclosure of collegium recommendations, or accountability, such as a judicial accountability bill, is antithetical to judicial independence. That is frankly an indefensible understanding of independence. Judges

must be independent, but they must also be accountable, impartial, and men and women of integrity. To take out one value and elevate it to the level of dogma, I argue in my book, is the reason why we are where we are today.

**Has the higher judiciary become a law unto itself, given how it has walled out scrutiny? It provides self-regulation in the name of separation of powers.**

One would have hoped that if it is a law unto itself, that law it would follow would be the law of the land! But we have seen time and again this is not the case. Take the National Judicial Appointments Commission case. There were several issues with the NJAC Act that was passed by Parliament. Those could have been read down. But to say that judicial primacy in appointments is part of the basic structure of the Constitution at the same level as federalism, secularism and the rule of law is a trifle mind-boggling.

It's a product of a mismatch between the accountability it owes and the power it enjoys. Over last two decades, judges, particularly of the SC, have become very prominent in everyday public discourse. With such visibility, the demands for accountability are natural. The SC has to introspect—if it wants to wade into governance issues ranging from NRC to BCCI to liquor vendors on the highway, then it must be open to greater scrutiny, questioning and attention. It cannot rest on antiquated notions of convention and intrinsic integrity. Instead, if it wants to stick to time-tested convention, then it should do what judges are theoretically supposed to do—like umpires, decide disputes, and leave the actual matter of governance to players, i.e. the government.

**Justice AP Shah says the problems highlighted at the Four judges conference—while current CJI Ranjan Gogoi and three other senior SC judges accused then CJI Dipak Misra of sitting in judg-**

ment of cases pertaining to Misra, something that is mirrored in how Gogoi has dealt with sexual misconduct allegations against him—weren't particular to Misra's tenure as CJI, that this has been happening for years...

I'm not aware of the facts Justice Shah is referring to. But the controversy pertaining to the CJI as "master of the rooster" is another example of old world convention operating in a changed world. The CJI and all chief justices the world over whenever courts sit in benches have to allocate cases. If you can't trust the CJI to do that, then the person should not be CJI in the first place. But once a CJI, one can expect basic functions of this nature will not be questioned. This is not helped by the fact that both Misra and Gogoi have, in some sense, acted as judges in their own cause. When events like this happen, the effects aren't felt immediately but the damage is lasting. The unfortunate outcome of both these episodes, irrespective of the merits of the cases, is the office of the CJI is no longer immune to doubts, gossip and speculation. This is an unfortunate development, but the writing was

really on the wall for a long time.

**Does the collegium system, brought in the name of separation of powers and independence of the judiciary from the executive arm of the government, of appointment to the higher judiciary, enjoys the backing of the Constitution, however indirectly?**

As I've argued in my book, the collegium has no constitutional basis. It was never intended by the framers who were categorical that the power of appointment belongs to the President who will ultimately be guided by the aid and advice of the Council of Ministers. Even in the immediate aftermath of the Emergency, the SC comprising stalwarts like Justice PN Bhagwati and Justice DA Desai refused to interpret Article 124(2) dealing with appointments to the SC to

require a collegium. It is also not a practice anywhere in the world that judges are focally responsible for selecting judges. The Constitution was interpreted in this manner in the *Second Judges' Case* because Justice JS Verma believed judges alone will be able to protect judges. As I've written in my book, "he created an institution with weak normative foundations, based on an unquestioned faith that the judiciary would be ideally placed to set its own house in order. Little did he realise then, that this act of judicial arrogation of appointment power, notwithstanding its noble intentions, would itself fall prey to undue influence and interference, tarnishing the image of the judiciary as well as questioning his own wisdom in adopting such a course of action."

**The striking down of the NJAC Act as unconstitutional was a blow to what you have termed the goal of nurturing an "an effective judiciary", one that is independent, yet accountable. How do we correct that? Is it for the judiciary to correct its own course, or should a course-correction, even if it is terms of oversight like what was proposed in 2010, be legislated?**

In terms of how the judicial appointments system can be changed, there is only one way—constitutional amendment. But it will be a difficult amendment given that the SC, whether rightly or wrongly in the NJAC case, has held judicial primacy in appointments to be part of the basic structure. So perhaps it might have to be an NJAC with a majority of judges combined with a transparent and publicly declared process of appointment. But this doesn't mean the judiciary must not self-correct. It is always open to the judiciary to do so. This is what Justice J Chelameswar was advocating when he decided to not participate in collegium meetings batting for minutes to be recorded and proceedings to be transparent. But at that time the SC resisted and was aided in this by senior members of the Bar like Fali Nariman who said that the "citadel collapses from within" which stalled any reforms. So if the SC can introduce genuine transparency in selection process, have a fair method of conducting disciplinary enquiries and transfer judges only on basis of recorded reasons, those will all be meaningful changes.

**Beyond the conduct of the judiciary, the problem of accountability also relates to punishment of erring judges. There are instances of allegations of corruption against High Court judges earning them, at the very worst, a transfer. The impeachment process is tedious and lengthy, one that inspires no confidence. What are your comments?**

You're right. There are no serious consequences for judicial misconduct short of impeachment. This is because the thought of High Court and SC judges indulging in misconduct was anathema to the founding fathers of the Constitution. The very thought could not be entertained! Today we are living in a completely different world, but the law is frozen in time. And we need measures to deal with that. The Judicial Standards and Accountability Bill conducting mechanisms for dealing with misconduct short of impeachment—such as suspension, censure etc—is one method that I suggest. There are many more.

The churn and disquiet that we see around us today relating to the higher judiciary is unfortunate. But at the same time whenever there is a churn, there is a period of tumult. We are living in that period now. The judiciary is slowly but surely changing from a colonial institution steeped in convention to a more Indian institution that is comfortable in the rough and tumble of India's noisy democracy. I expect the churn to continue for a decade or so, but after that we will find a judiciary that has regained public confidence not through secrecy and awe but through understanding and respect. I say this, both with hope and certainty, that such a day is not far away.

*'Independence and Accountability of the Indian Higher Judiciary' is written by Arghya Sengupta and published by Cambridge University Press. It releases on May 9, 2019, at 6:30 pm at the India International Centre, New Delhi*

## Anchoring bias in investments

VIPUL PRASAD

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Awareness and assessment can act as the first line of defence

**T**HE IMPORTANCE OF BEHAVIOURAL finance in fundamental investment process is difficult to overstate. Anchoring bias is a common behavioural heuristic that often prompts investors to make poor decisions. Seeds of this bias are sown when someone assumes certain value for an unknown quantity before attempting to estimate that quantity. Bad outcomes follow when one is unable to dissociate from this assumed value even after receiving new information. Here are some examples of anchoring bias in investments:

**False assumption of missed opportunity:** Let's say an investor considers buying a stock at ₹100. While he is analysing the stock, it rises to ₹115. The analysis concludes that the stock can rise to ₹170-180 over the required investment horizon of, say, two years. In another scenario, the investor rejects the stock at ₹100, but after some time—when the stock has appreciated to ₹115—he takes a relook and realises that the stock has massive upside.

In both these situations, the investor may now, owing to anchoring bias, wait for the stock to slip closer to ₹100 before he buys it. The problem is he anchored himself to the price of ₹100 where the stock was when he considered it initially. But instead of getting hooked on to the notional loss (of ₹15, i.e. the difference between purchase price and the price when he first considered the stock), the investor should focus on the potential upside (48-57% as per his analysis, i.e. the difference between purchase price and fair value of the stock).

**Chasing up a stock:** This situation is commonly encountered after a false assumption of missed opportunity. Let's say, as earlier, after rejecting the stock at ₹115, the investor again investigates the stock at ₹130 after coming to know that his friend bought the stock at ₹115. Due to the 'missed opportunity' syndrome, he again refrains from buying the stock. He has been monitoring it closely and thinks of buying it at ₹150, but concludes, to an extent rightly, there is not much upside left. He has also been checking his friend's hefty returns. Eventually, in a dash of greed and recklessness, he buys the stock at ₹165, even though his dispassionate analysis pegged the potential upside at a maximum of 5-10%. But anchored to his friend's stock return so far, of about 45%, he somehow flexed his valuation model to suggest, mistakenly, further upside potential of 30-40%. The mistake here was he got triggered to past stock returns, and to the profit made by his friend. Had he maintained focus on his real anchor in the circumstances, he would have done the stock's fair value calculation to estimate his future return.

**Buying after a steep fall, or at 52 weeks low:** Often, one buys a stock just because it has fallen by 20-30% in, say, last 3-6 months. Here the investor is incorrectly anchoring to the stock price prior to the decline, or to the price trend in the last 52 weeks. In reality, the stock may have reasons to fall more incrementally and the right anchor should be the fair value of the stock. For example, in a majority of the stocks in India that fell by 20-30% in 1H2018, actually fell further in the second half of the year, too—many are still languishing not too far from their lows, with dim future prospects. Indeed, there is no harm in starting with such filters, but it is extremely important to analyse the stock fundamentally from all aspects before making an investment decision.

**Waiting for break-even:** There are occasions where even if one does not like a stock any more, one continues to hold it, hoping for a break-even. Since the investor had purchased the stock at ₹100, he is essentially unwilling to sell it at ₹97—even if he does not like it. If he were to behave rationally here, he would compare the current stock price of ₹97 to the fair value (say, at ₹75) and not to the purchase price (₹100).

**Selling too early:** If an investor purchased a stock at ₹200 with an assessment it would grow to ₹200 over three years, he should not sell it after appreciation of 33% in one year—unless there is a change in the stock thesis and hence in incremental upside expectation. Else, the investor would wrongly take the purchase price as the anchor, whereas he should concentrate on the fair value. If the stock looks good to hit ₹200 over next two years, even after it has reached ₹133 in the first year, it will be a poor move to sell it there.

While there is no clear-cut formula to overcome anchoring bias in investments, awareness and assessment can act as the first line of defence. It is important to disconnect oneself from past stock trends, or purchase price, and instead to focus on fundamentals and on the stock's fair value. The key is to spot our brain's urge to take the easy and fast route in such situations, leading to mistakes. To avoid falling victim to anchoring bias in investments, one needs to use templates from the past as well as from other disciplines and assess multiple options before arriving at an investment decision.

**T**HOSE FAMILIAR WITH the growth story of the corporate sector know how corporations, big and small, owe a great deal of their ability to dream big and achieve success to a strong supporting ecosystem—funders who provided capital to get ideas off the ground, consultants who provided strategic inputs, recruiters who helped get the right talent, specialists who helped build organisational capability, and so on. It took many actors in an interconnected ecosystem to enable businesses to achieve their potential.

At a critical time in the history of India's social sector, an 'ecosystem' of this kind will decide how the sector grows in the years ahead. At the moment, though, this ecosystem is still an idea being discussed, sometimes vaguely, by a handful of people in the social sector. So, what is this 'ecosystem' we are talking about, why do we need it and, importantly, who is to build it?

As in the corporate sector, a set of intermediaries who create transparency and enable better decision-making is critical to India's non-profit sector at this juncture. There is a range of possibilities and roles for these intermediaries but, to my mind, the most critical are those involved with talent and capital.

Let's use a parallel from the Indian venture capital industry, where an influx of capital from the likes of Sequoia, SoftBank and Tiger allowed our entrepreneurs to

## Building ecosystem for the social sector

Philanthropists must encourage testing of innovative models, making more risk capital available to non-profits

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capital bigger than ever before. But as the capital came in, we also saw a situation where there was so much more to do, but not enough talent to seize those opportunities. Similarly, as the non-profit sector is poised for a phase of growth, talent could be one binding constraint in the near term.

The huge influx of capital, especially the ₹50,000 crore from CSR in just five years, has dealt a comparable kind of shock to the non-profit system. Domestic philanthropy has also seen a surge: who would have thought Azim Premji would give away another \$20 billion! Whilst there isn't, obviously, another donor of that size, many more people are now committing to give money and are willing to be much more active participants, not just donors,

in the process of social development.

Just as venture capitalists demanded more accountability from Indian start-ups—the reason today's start-ups are more professional than those of 20 years ago—today's donors demand better processes, better utilisation of funds and more professionalisation within non-profits. Having built successful for-profit companies, individual philanthropists are now demanding that non-profits focus on the talent piece. People like Amit Chandra, for example, focus specifically on capacity building grants. CSR is also demanding systems, processes, auditing, governance, etc. And so, this is the moment when the social sector needs to respond.

We are already seeing how organisa-



tions that have responded to these demands have grown rapidly. The likes of Magic Bus, Kaivalya Education Foundation and Teach For India have grown tremendously in the last five years because they realised they could tap into this pool of capital if they did the right things, hired good talent and professionalised.

Talent will have to be the single biggest investment in this sector, going forward. We're at a stage where good quality junior talent has started coming into the sector. What we will also need is a leadership pipeline; it's going to be almost impossible to build the leadership and skills from within organisations in a short span of time. Which is why we now see initiatives like India Leaders for Social Sector to bring

in experience, talent and skills from the corporate sector. Another area where the social sector needs expertise is evidence, monitoring and evaluation, and reporting. If we want the quality of the sector to improve, we should demand more rigorous evaluation to determine whether something is genuinely working or not. Unless we see more rigour on this front, we will continue to compromise our ability to take informed decisions regarding our response to societal problems.

We have a gap in terms of the information available in the public domain regarding how much philanthropists are giving, where they are giving, etc. I don't think there are enough intermediaries that have done a good job at making such data avail-

able. Apart from more rigorous evidence, we also need evidence that is more readily digestible so that people don't make the same mistakes they made 20 years ago.

Like Pratham created ASER, there is a need to create similar tools or public good that transcends their limited scope within programmes and organisations to become useful to different organisations, across sectors. That way, governments and organisations get access to a ready set of tested tools and won't need to reinvent the wheel.

The question, of course, is what will it take to build such an ecosystem? Philanthropy certainly has an important role to play here. Rather than fund organisations to just do more of what they're doing, philanthropists must be willing to encourage testing of innovative models, making more risk capital available to non-profits.

Donors must make budgets available for capacity building and not just for programmes. As organisations grow, donors need to be okay with, say, 20-25% of their grants going towards 'administrative costs' of grantee organisations, including investments in human capital, M&E, marketing, brand building, fund-raising, technology and systems.

As India's non-profits negotiate the opportunities that come with increased investment and interest, our ability to put in place an enabling ecosystem will be the key that decides how well, how quickly and how effectively they respond.