Boeing and its future

The recent two crashes could lead to better coordination between regulators and thorough review of the certification processes

TECH-ENABLED

DEVANGSHU DATTA

The latest news about Boeing's 737 Max indicates the grounded airliner could have more defects that may lead to it being indefinitely grounded. Two fatal crashes have been attributed to a flawed software controller system, the MCAS (Manoeuvring Characteristics Aug_mentation System), which is undergoing a complete overhaul.

In addition, there may have been faulty microprocessors that compounded the MCAS issues with the MCAS, and there may be defective wing components that will need replacement in many aircraft of the 737 class, including the Max series.

The Allied Pilots Association is considering suing Boeing. The American safety regulator, the Federal Aviation Administration (FAA), may end up reviewing its certification processes. Other national aviation safety regulators may either check the 737 Max independently, or coordinate with the FAA during the re-certification process as the EU, Brazil and Canada are doing.

The MCAS was designed to prevent stalling. In wind tunnel experiments, Boeing engineers had discovered the aircraft tended to stall when the "angle of attack" hit a certain level. The angle of attack is the angle made by the wing and oncoming airflow — this varies as the nose is pointed up or down during flight. The MCAS was supposed to diagnose when the angle hit unacceptable levels when it would activate a physical control in the tail, pushing the tail up and pushing the nose down.

Problems with MCAS led to the Ethiopian Air and Lion Air crashes where 346 people died. The MCAS is designed to activate on the basis of data from sensors that monitor air speed, and angle of attack, and so on.

But it can activate on the basis of false data from a single faulty sensor. In both crashes, it was triggered by a single sensor and the MCAS repeatedly forced the nose down even though the planes weren't stalling. That caused steep dives. A rejig of the software will involve the MCAS being modified to ensure that a single sensor cannot trigger the system; it will have to be based on data from at least two sensors.

There were other issues with the MCAS. One was that it assumed the pilot could take corrective action within three seconds. This time span is based on the FAA regulations but it may be too short. Boeing is likely to reduce the power of MCAS as well as to try and obviate steep dives.

Boeing was in a hurry to get the Max series certified and cut corners in terms of explaining it to pilots. Pilots trained on the earlier 737 series, which did not have this problem, were given training on an iPad programme rather than a full simulator. The aircraft was offered at a substantial discount to airlines, which did not insist on simulator training for pilots.

Hence pilots did not know much about MCAS and indeed, the two crashes may have occurred due to their being unaware of the MCAS and unable to shut it down and take manual control. Senior pilots who have tested the system subsequent to the crashes say that surprised pilots may have taken too long to cope with the emergency. This lack of briefing and training are asking the reasons why pilots are threatening legal action against Boeing.

In simulator exercises after the crash, pilots also discovered that microprocessors failure could lead to nosedives. Although faulty microprocessors may not have been responsible for the fatal crashes, there would have to be physical inspections of the MCAS hardware and failsafes must be built into the new MCAS system which Boeing is working on.

A new component fault has surfaced. A component called a leading edge slat track that is placed on the wings may have been defective in several batches of 737 Max and the earlier 737 NG series. Although the company claims this is not dangerous, these components are being checked and replaced, with Boeing issuing an advisory for airlines using NG series (these are not grounded). This component is used to control the aerodynamics of the wing surface and if these slats crack, or prove to be faulty, there would be damage to the aircraft. The FAA has asked airlines to carry out inspections within 10 days.

The one outcome of those two crashes is that it could lead to thorough review of the certification processes and better coordination between regulators. It's likely that pilots will receive better training in future. Boeing has suffered huge loss of reputation and taken a beating at the stock market as the damaging information had surfaced. This would also be a disincentive for aircraft manufacturers to cut corners in future.

CHINESE WHISPERS

Water politics

As the water crisis worsens in Chennai, many are using this commodity as a marketing tool. While brawls over a pot of water are common now near water tanks, it even costs around ₹15 a pot when one buys from private tankers, some of the shops have started offering a pot of groundwater free with a kg of dosa/idli batter. "Please bring an empty pot when you come to buy batter," says a poster outside a store in the city. Many families are opting to eat from restaurants as there is no water for cooking and washing utensils in the house. Considering the negative public sentiment and a possible hullabaloo from the Dravida Munnetra Kazhagam (DMK) in the Assembly, the ruling All India Anna Dravida Munnetra Kazhagam (AIADMK) has mandated that none of its members can skip the session. The AIADMK needs its maximum strength in the House to face any argument and to show each of its members are serious about the crisis. There were rumours of a no-confidence motion moved by the DMK against Speaker P Dhanapal. However, DMK leader M K Stalin has clarified that there'll be no such motion as the issue has become old now.

Divided house

The Congress party's confusion over its leadership question has affected its strategy in Parliament as well. Senior MPs from the party concede they are at sea on the position to take on important issues. Leaders like Ghulam Nabi Azad in the Rajya Sabha and Manish Tewari in the Lok Sabha, have dipped into their experience to save the party from embarrassment on occasions. The Congress party's lacklustre approach has given the Trinamool Congress (TMC) the space to drive the Opposition strategy in the two Houses. The latest example has been the TMC pushing for a discussion on electoral reforms. The party reached out to other Opposition parties, as many as 14, to get them to convince Chairman M Venkaiah Naidu to hold a short duration discussion.

Help but no help

The former Bharatiya Janata Party-led government in Madhya Pradesh had started a CM helpline, one of its flagship programmes, with much fanfare in 2014. But it has lost its appeal. The helpline was meant for addressing public grievances with a one-touch complaint system. However, according to official data, 0.3 million complaints lodged in the CM helpline are pending with various government departments. The revenue department has the maximum number of pending complaints — 45,000. Sources said that most of the pending cases were registered in the last seven months. The new Congress-led government has shown no interest in solving the complaints but haven't admitted it publicly.

Banking on the Union Budget

PSB privatisation is a bold idea and for a government that embraced demonetisation, it could be a cakewalk

BANKER'S TRUST

TAMAL BANDYOPADHYAY

In the run up to the Union Budget, all industry bodies reach out to the North Block with their agenda. For the banking industry, this annual ritual, typically focuses on the unlevel playing field vis-à-vis mutual funds and the government savings schemes. Banks find it difficult to bring down the interest rates on deposits for fear of losing out to the mutual fund schemes that offer certain tax benefits and the high-yield government savings schemes. Ahead of this Budget, the government has cut the interest rates on small savings schemes and the market regulator's new rule may force corporations to move part of their funds from mutual funds to banks.

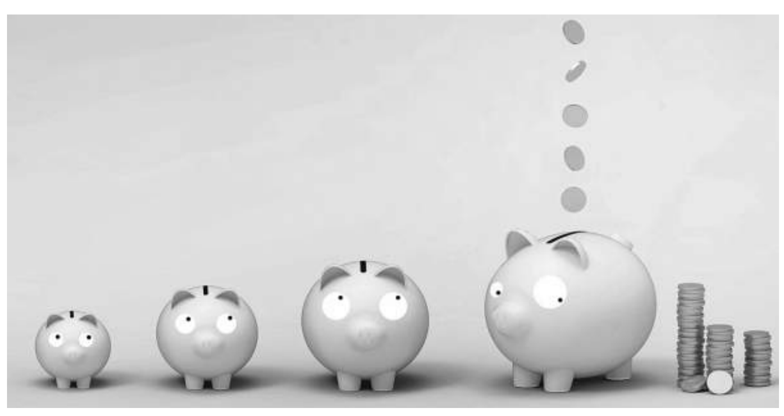
So, what should Finance Minister Nirmala Sitharaman do for the banking sector? Here are a few suggestions — not exactly unsolicited as she had asked for them on Twitter. While keeping the tradition of meeting the industry lobby groups and economists alive, the Bharatiya Janata Party-led National Democratic Alliance (NDA) government has started crowdsourcing inputs for Budget since 2016. I have missed the deadline for submission of such suggestions but am still joining the crowd.

For quite some time, the talking point at the cocktail circuit has been the risk averseness of the public sector banks (PSBs) — they don't want to give loans. The root of it is a fear psychosis. The investigative agencies have been hounding senior bankers and barring an odd case of the CEO of a private bank, they are particularly aggressive when it comes to officials of the government-owned banks.

Quite a few of them have been arrested and many more questioned but there has not been a single instance of a public sector banker being prosecuted for mala fide decisions on giving loans or settling the dues of a defaulter. The fear is slowing down both lending as well as recovery of bad loans. It's time to instil confidence in these bankers who run close to 70 per cent of the industry. Indeed, the guilty should be punished but just based on allegations they should not be harassed and their reputation sacrificed.

While bankers at the senior level should be under strict surveillance, they also need to be rewarded suitably. Let's delink the salary structure of PSB chiefs from that of the civil servants as their job profiles are different. And, there should be incentives for performers. The employee stock options proposals of at least two banks — State Bank of India and Bank of Baroda — have been gathering dust in the North Block for years now.

A strong banking system is imperative for economic growth and the bad loan-laden PSBs cannot play a meaningful role. The recent crisis in the non-banking finance sector has intensified the problem and many banks are staring at potential fresh non-performing assets. The traditional tool to tackle this has been infusion of capital into these banks. Historically, the government has pumped in ₹3.5 trillion, a bulk of which (some ₹3.3 trillion) has come in since 2009.



A strong banking system is imperative for economic growth and the bad loan-laden PSBs cannot play a meaningful role. The recent crisis in the NBFC sector has led to banks staring at potential fresh NPAs. The traditional tool to tackle this has been infusion of capital into these banks

In the past two years alone, the government has infused close to ₹ 2 trillion to keep the ailing PSBs afloat. For the record, since fiscal year 2016 when the Reserve Bank of India introduced the so-called asset quality review (AQR) to clean up banks' balance sheets, the PSBs have made net losses of ₹1.78 trillion. In the five years of the NDA rule, between financial year 2015 and 2019, the PSBs made losses in three years, and the profits made in two years is less than ₹35,000 crore.

The reason for the huge losses is over ₹9.2 trillion provisions that these banks needed to do in these five years to take care of their bad loans. The gross bad loans of the PSBs that were ₹2.62 trillion in 2015, jumped to ₹5.16 trillion the very next year following the AQR, and ₹8.96 trillion in 2018, before sliding to ₹7.68 trillion in 2019. Two PSBs now have at least one-fourth of their loan assets stinking; for one of them, bad loans are at least 20 per cent of the loan book; and for nine, at least 15 per cent. The growth in interest income is muted as many of these banks are not able to give fresh loans. While net losses have zoomed in the past five years because of bloated provision requirement, their net interest income has risen progressively from ₹1.81 trillion in 2015 to ₹2.3 trillion in 2019.

Should the government continue to own all these banks? Is consolidation the panacea? Former finance minister Arun Jaitley had committed to privatising the sick IDBI Bank and this has been done. The government is no longer the majority owner of this bank. Life Insurance Corporation of India has stepped in as the new owner. Is this privatisation? The consolidation drive started with merging the associate banks with the nation's largest lender, the State Bank of India. While that was a sort of family affair, the merger of two PSBs with Bank of Baroda demonstrates the seriousness of the government's intent. Will this solve the problem? Do we need so many PSBs? Can all of them be merged into different groups to form large banks?

A panel has recommended creation of a holding company for all PSBs by transferring the government's stake to it to run them efficiently and create value. Recent media reports suggest that this proposal has been revived. This may not work as it's difficult for the government to give up its control. The best solution is amending the Banking Act that says the government must hold at least 51 per cent of the paid-up capital in such banks and privatise a few of them.

Some of the weak banks have rotten balance sheets but they are great liability franchises. That's a perfect match for some of the troubled non-banking finance companies (NBFCs) that have been suffering from acute liquidity problem, which is threatening to affect their solvency. Why not auction some of the weak banks to the highest bidders? Of course, the prospective buyers must meet the so-called fit and proper criterion for owning and running a bank.

The government can make money selling even weak banks as the distressed NBFCs need robust liability-raising network and the money generated can be pumped into the not-so-weak banks to nurse them back to health. Done this way, the PSB recapitalisation will not have any impact on the fiscal deficit.

This is a bold idea but for a government that embraced demonetisation, it could be a cakewalk.

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AS I SEE IT

Is the Opposition falling apart?

KARAN THAPAR

After the Bharatiya Janata Party's (BJP) phenomenal victory and its own crushing defeat, I've started to ask myself a disturbing question: Is the Opposition falling apart? I can't answer conclusively but I also can't deny there are clear signs it is. What's worse is that the disintegration that's distinctly visible is likely to get worse.

Let's start with the big picture. The Congress has gone into a crisis, in UP the *gathbandhan* has split, in Andhra and Telangana the Opposition is merging with the BJP or the TRS, in Karnataka the Congress-JD(S) government is in danger of collapsing and in West Bengal, Mamata Banerjee is showing undeniable signs of panic. From the Hindi heartland to the south, but also the east and, of course, Delhi the cracks are spreading. Opposition unity ended with the elections. Now individual parties are either paralysed or splitting.

The most dramatic is the paralysis that's seized the Congress after Rahul Gandhi's decision to resign. He insists on going but the party persists with the hope they can change his mind. As a result, instead of leadership the party has a vacuum at the top.

The view from the states is, at least, as disturbing. Already Deve Gowda has voiced his fear the Congress-JD(S) government in Bengaluru could fall. But there are also gathering clouds on the horizon in Bhopal and Jaipur. Doesn't that suggest things could get a lot worse for the Congress in the weeks and months ahead?

The picture in UP and, possibly, Bihar is equally distressing. In the former, the collapse of the *gathbandhan* has ensured that the forthcoming 11 by-elections will be a four cornered fight. That can only be good news for Chief Minister Adityanath who can now look forward to winning all of them. Meanwhile, the bitterness between SP and BSP is more likely to make them quarrel with each other than effectively challenge the BJP.

Now there are hints of a similar falling apart in Bihar. The Congress leaders in the state are talking of going their own way and deserting the RJD. I don't know if that will happen but, equally, I can't confidently say it won't.

Finally, developments in Telangana and Andhra are hardly reassuring. In both the states, the Opposition party has split and either merged with the TRS or the BJP. Consequently, both look like one-party states and neither has an effective Opposition.

Perhaps the only Opposition leader who's determination and focus hasn't wavered is Mamata Banerjee. But her behaviour over the doctors' strike and, earlier, over the *Jai Sri Ram* episode is more likely to strengthen Modi's BJP than her own TMC. If she isn't careful she could actually end up cutting the ground from under her feet.

If this wasn't bad enough, the future is unlikely to bring comfort. Elections are due in a couple of months in Maharashtra, Haryana and Jharkhand. Hasn't the crisis in the Congress ensured the BJP will comfortably return in all three and won't that hammer a few more nails into the Congress' coffin?

Infact, it's the Congress I'm most worried about. Once it accepts Rahul Gandhi's departure, could the party tear itself apart finding a new leader? Already the electoral crushing has sparked off serious factions fights in Haryana, Punjab, Madhya Pradesh, Rajasthan, Uttarakhand and Karnataka whilst provoking debilitating desertions in Maharashtra and Telangana. Or if the Congress manages to hang together under Gandhi protection — by asking them to function as the power behind the throne — won't that render the new president a puppet and the subject of derision?

It's electoral prospects are equally dire. With a solitary seat and just six per cent of the vote share, its very unlikely the Congress can revive quickly or easily in UP. And that's true of Bihar too. But the worst part is the Congress' presence may also be diminishing in the south. Its already irrelevant in Andhra and reduced to a rump in Telangana. It's on the back foot in Karnataka and only survives with DMK assistance in Tamil Nadu. Its only credible base is Kerala. But at this rate how long will it be before south India turns its back on the Congress?

If in these circumstances you still see signs of hope then, I guess, you must believe in the phoenix.

LETTERS

Not a viable solution

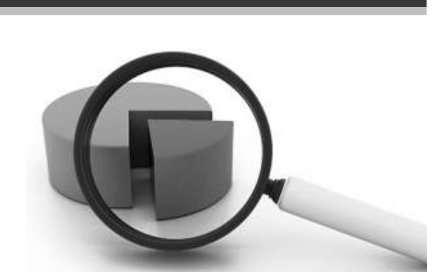
This refers to "If PSBs can't lend, they should be privatised" (June 29). It seems Niranjan Hiranandani's *(pictured)* panacea for lack of public sector banks (PSBs) lending is the privatisation of PSBs. The PSBs are not lending because their earlier reckless lending has turned into non-performing assets (NPAs). These NPAs are under-capitalised and the banks are restrained by the prompt corrective action framework as they do not meet the stipulated regulatory financial parameters. He says that "excessive funds lying with banks should be disbursed in the market". Banks are in the business of financial intermediation that is, prudent lending, so as to give a decent return to their depositors and pay dividend to their owners. They are not soup kitchens set up during natural disasters. Similar problems arose in the NBFC sector because some large non-banking financial corporations (NBFCs) got into dire straits. There are issues for mutual funds on account of defaults.

Mr Hiranandani should realise that weak and beleaguered financial institutions can't lend like healthy institutions. They need time to recuperate. They need comprehensive governance and operational reforms. Just by privatising the PSBs, the problems won't go away. What kind of valuations would poorly capitalised institutions with high percentage of stressed assets and outdated systems get in the market? Aren't some of the private banks facing governance and ownership problems? His argument of converting 4,000 NBFCs into banks, I presume, was said in jest. Banks are institutions holding public deposits and should have the trust of the public. Privatisation and reckless lending are not the solutions.

The Reserve Bank of India has taken appropriate steps both through its monetary policy and its liquidity management mechanisms to do the needful.

Arun Pasricha New Delhi

Let auditors do auditing



This refers to "A raw deal for auditors" (June 28). Auditors' report and comments have significant value to the investors, lenders, creditors of the business organisation, the regulators, taxmen and to the government. The frauds in banks and other business entities point that the authorities of those institutions exploited the vulnerabilities and intentionally committed fraud for monetary gains.

Albeit the system of inspection and oversight in vogue, fraud and embezzlement are not uncommon. It indicates that either the management failed to enforce supervision or colluded with the fraudsters. Keeping aside the auditing, if auditors go for investigations to unearth the criminal conspiracies, they will fail to submit the audited financial statements and report well within the specified time. They have a defined objective and accordingly, they have to audit the books of accounts and ensure that the organisation have complied with the norms of accounting and bookkeeping and the business policies of the entity. Any violation, deviation from the norms in force, suspicious transactions, and loophole in the system and procedure must find a place in the audit report. The audit report must maintain quality. The audited documents and reports are meant for the regulators and the stakeholders to enable them to take decisions on investment and other related matters.

The quitting of auditors from the audit work of many business entities exposes the unwillingness of the promoter or the management to provide information, data and clarification because of the fear of detecting violations of norms and regulations. However, such actions have adversely affected the investors manifold. Failure of the auditing team in detecting the conspiracy of the promoter or the management doesn't mean that the auditors are co-conspirators.

VSK Pillai Kottayam

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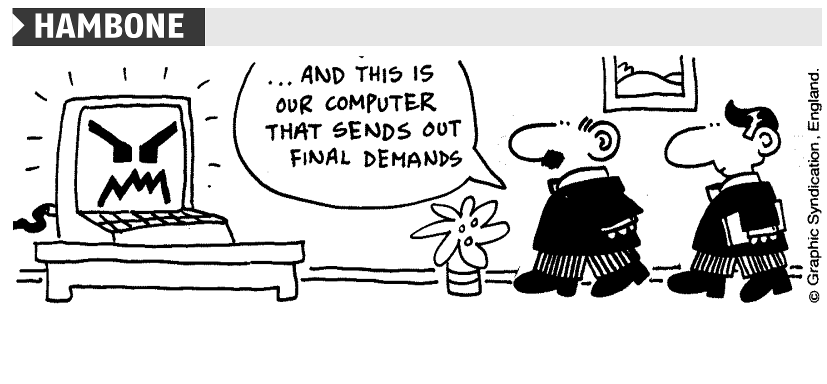
HAMBONE



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The good and the bad

Fog over bank NPA lifts, but shadow over NBFCs lengthens

Indian banks seem to have finally got a grip on their bad debt problem. The non-performing assets (NPA) cycle peaked in March 2018, thanks to the relentless drive by the Reserve Bank of India (RBI) over the past four years to make banks recognise their hidden bad assets. With most of the stress identified, the NPA cycle has turned around with the gross NPA ratio declining to 9.3 per cent in March 2019, and is expected to fall to 9 per cent in March 2020, according to the RBI's Financial Stability Report, released on Friday. Public sector banks' (PSBs') gross NPA ratio may decline from 12.6 per cent in March 2019 to 12 per cent by March 2020, while private sector banks may witness the ratio improving from 3.7 per cent to 3.2 per cent. The provision coverage ratio (PCR) of all banks rose sharply to 60.6 per cent in March 2019 from 52.4 per cent in September 2018 and 48.3 per cent in March 2018, increasing the resilience of the banking sector.

While the first "R" of "recognition, resolution and recovery" seems to have been realised, the harder part remains. The good news is that the Insolvency and Bankruptcy Code (IBC) is a strong regulation though resolution in some cases is still stuck in courts. Under the RBI's revised prudential framework on stressed assets issued in June 2019, there is a disincentive for banks in delaying to file insolvency applications. Interestingly, a systemic risk survey by the central bank found that half the respondents agreed that the prospects of the Indian banking sector would improve, albeit marginally, in the next one year aided by the stabilisation of the process under the IBC. That would also improve the confidence in the domestic financial system, according to the FSR.

However, it is important for banks to realise that they can no longer continue doing business the old way. The FSR also points out that at least five banks would be falling below the regulatory level of minimum capital adequacy by next year if no additional money is infused by the government. In any case, recapitalisation of banks can be only a temporary fix, while the permanent solution would be to merge these weak banks into a larger entity that can be managed better and more efficiently.

The bigger problem is the health of the non-banking financial companies (NBFCs). The gross NPA ratio of the sector increased from 5.8 per cent in 2017-18 to 6.6 per cent in 2018-19, while the capital adequacy ratio moderated at 19.3 per cent from 22.8 per cent in March 2018. And on top of that, some of the NBFCs are defaulting or delaying on their payment obligations. According to the RBI's contagion analysis, should the largest housing finance company fail, it can wipe out 5.8 per cent of the tier-1 capital of the banking system. The RBI sought to brighten up the mood by saying that the sector had been brought under greater market discipline as the better-performing companies continued to raise funds while those with asset quality concerns were subjected to higher borrowing costs. But that may not be enough; the regulator needs to think about proactive steps to help prevent a contagion risk.

Reforming small savings

Interest rates should be linked to market outcomes

The government has lowered the interest rates for depositors in various government-run small savings schemes, including the National Savings Certificate (NSC) and Public Provident Fund, by 10 basis points for the July-September quarter. Savings deposit rates have, however, been maintained at 4 per cent annually. The NSC will now fetch an annual interest rate of 7.9 per cent from the existing rate of 8 per cent, while the Kisan Vikas Patra will yield 7.6 per cent with maturity of 113 months. The government deserves credit for this move towards rationalising the interest rate transmission mechanism, in line with the promise in its manifesto for the 2019 general elections to "structurally lower the real cost of capital".

The Reserve Bank of India (RBI) has now cut the headline repo rate three times, by 25 basis points each time. Thus, the repo rate is now 5.75 per cent. But the benefits of these cuts have not been fully passed on to borrowers. Many banks have argued that they are seeing competitive pressures from small savings schemes. For small savers, the schemes provide super-normal returns, thanks to the administered interest rate regime they are under. Thus, many prefer them to bank deposits. This means that banks cannot allow the spread between the rates they offer depositors and the rates published for the small savings schemes to grow too great. If the banks are thus constrained to offer higher rates to depositors than they normally would, there is a floor under which they will struggle to go in the rates they offer borrowers in turn — regardless of how often or how much the central bank cuts the repo rate. This is a severe handicap when it comes to monetary policy transmission, and it is one that has been pointed out by the RBI often enough.

The latest cut in the rates available to depositors in the small savings schemes should only be a first step. Interest rates across different segments should be automatically set to align with market-determined rates, so as to ensure that monetary policy transmission occurs seamlessly. The point behind small savings schemes is to allow savers access to low-risk opportunities by depositing their savings with the government. In other words, the rates these small savers are offered should be in line with the yields on government bonds. Unfortunately, political considerations frequently mean that the administered interest rates do not reflect changes in the yields on government bonds, which are driven by market forces. For example, the decline in yields on g-secs in the months leading to the election was not reflected in a change in the administered interest rates.

That the cut is not enough is evident from the fact that while bonds yields are down about 40 bps in the relevant quarter, the cut in small savings rates is just 10 bps. The government should, as soon as possible, put in place a formula for determining the returns on small savings schemes that directly link those rates to the yields on government securities emerging from the secondary bond market. This will remove political pressures from decisions and allow for smooth and seamless monetary policy transmission.

Lower the corporate tax rate

Small changes in taxation can kick off disproportionate responses by way of shifts in capital

SNAKES & LADDERS

AJAY SHAH

India is unusual, when compared with emerging markets or the G20 countries, on the high taxation of corporate profit. The Indian corporate tax rate was higher than the G20 median, by about 9 or 10 percentage points, in 2001, 2005, and 2006. After that, India's gap has risen to 21 percentage points, as corporate taxation has declined the world over. India gains by reducing corporate taxation as this improves the appeal for investing in India for local and foreign persons, it reduces double taxation of the corporate form, and it generates increased property and tax revenues through indirect channels. This process had begun in 2015, and needs to be featured in the July 5 speech.

The Organisation for Economic Co-operation and Development (OECD) runs a measurement system which shows the total taxation of the income of corporations. On June 27, Krishna Kant and Sachin P Mampatta *<a href="https://www.business-standard.com/article/economy-policy/at-48-3-in-2018-corporate-taxes-in-india-among-highest-in-the-world-119062700062_1.html">* wrote about this in *Business Standard*. India stands out in two respects.

In 2018, India stood at a high rate of 48.3 per cent. This was out of line when compared with the median emerging market (EM), which was at 25 per cent, or the median G20 country (27.7 per cent).

India is also out of line in the lack of change, over the years. In 2000, the Indian rate was at 48.1 per cent, which is essentially the same as where we are today. But over this period, the median EM dropped rates by 5 percentage points and the median G20 country dropped rates by 7.3 percentage points. This has made India stick out, to a greater extent, as a high-tax jurisdiction.

It is striking to see that the Indian gap, over the G20 countries, was at its lowest values in 2001, 2005, and 2006. This was the period when a great business cycle expansion ignited. We do not for a moment wish to suggest that there is a monocausal explanation that improved tax competitiveness sets off an investment boom. Many elements of policy-making went into India's remarkable period from 2002 to 2008. It is likely that tax competitiveness was one of them.

Why is this an important issue? There are three arguments in favour of low taxation of corporations. The first principles idea is that we should focus on taxation of individuals. Let's measure the total income of each individual, and apply a personal income tax on it. Once this is done, there is no need to additionally tax the organisational structure adopted through which the income is generated, whether it is a partnership or a proprietorship or a limited liability company. By penalising the corporate form, we give incentives for businesses to be organised in other ways, which is inefficient for the economy. Rules demanding substantial dividend payouts by corporations can ensure that corporate profits show up as personal income, where personal income tax is applied.

The second key insight is about the mobility of capital. Taxation of capital or of financial transactions works poorly because these markets are quite mobile. In the modern world, Indian and global holders of capital choose from a global menu of options for investment. Small changes in taxation can kick off disproportionate responses by way of shifts in capital. Shifts away from India, in the patterns of investment, are particularly harmful for India as we require a vast amount of investment to achieve prosperity.

This is why the right focus of tax policy in India should be upon three elements of the economy where flight of activity is difficult, ie

(a) the property tax,
(b) the consumption-based GST, and
(c) the residence-based personal income tax. All other attempts at taxation are termed 'bad taxes' as they lead to large changes in behaviour, which are not good for the country.

The third key insight is that the country and the government gain amply when an Indian or global corporation chooses to place operations here in India. The prosperity of the people of India goes up when firms decide to operate here. In addition, the government gets more tax revenue. Corporations that rent or buy property generate improved property tax revenues. Corporations that buy labour generate personal income tax, both at the first round effect (corporation hires one person) and through downstream impacts (this person buys a biscuit, and that generates personal income in the seller of biscuits). The Indian residents that obtain income from the corporation will turn around and consume, which generates GST revenues as the GST is a consumption tax based on a destination principle.

These three ideas have generated a historic movement, all over the world, away from high taxation of corporations. The average global corporate tax rate has steadily declined since 1980. Even in rich countries with an expensive welfare system, where large tax/GDP ratios are required, the focus is on getting the money through the three good taxes only (the GST, the personal income tax, and the property tax).

We should not be content with matching the median values of emerging markets. We should be competitive with world standards. The 25th percentile value among emerging markets is 20 per cent. Thus, if India goes to a 20 per cent corporate tax rate, we will be better than three-quarters of emerging markets. In particular, we will be more attractive than China, where the rate is 25 per cent.

In 2015, such an announcement was made, with many future dates on which the announcement would take effect. This led to a tepid response on the part of domestic and foreign investors, and their scepticism was proved right by the lack of follow through. It would be efficient for the July 2019 speech to introduce this action effective right now. This might generate some fiscal stress in 2019 and 2020. With a lag, the gains would kick in.

This is comparable to the thought process of cutting customs duties, from 1991 till 2003, where tax officials steadily protested the loss of tax revenue, but this was amply compensated by the economic dynamism that came from removing protectionism.

The writer is a professor at National Institute of Public Finance and Policy, New Delhi

A COMPARISON

Year	India	Median EM	Median G20	Gap for India against median EM	Gap for India against median G20
2000	48.1	30.0	35.0	18.1	13.09
2001	43.9	30.8	35.0	13.1	8.9
2002	45.1	30.0	34.5	15.1	10.55
2003	44.1	30.0	34.0	14.1	10.09
2004	44.9	30.0	33.5	14.9	11.38
2005	43.0	29.0	33.5	14.0	9.46
2006	43.3	28.0	33.5	15.3	9.87
2007	45.2	27.0	33.5	18.2	11.73
2008	45.2	25.0	30.0	20.2	15.21
2009	45.2	25.0	29.7	20.2	15.52
2010	44.3	24.2	29.7	20.1	14.57
2011	43.4	24.2	29.8	19.2	13.63
2012	43.4	24.2	29.8	19.2	13.61
2013	45.2	25.0	29.8	20.2	15.38
2014	45.2	25.0	29.9	20.2	15.35
2015	47.9	24.2	29.9	23.7	18.03
2016	47.9	24.0	29.9	23.9	18.02
2017	47.9	24.2	28.8	23.7	19.1
2018	48.3	25.0	27.7	23.3	20.66
Overall change	**0.2**	**–5**	**–7.3**	**5.2**	**7.57**

Source: OECD and author's calculations

Rethinking circular economy

DOWN TO EARTH

SUNITA NARAIN

I am inside a dark and dingy "factory", looking at plastic waste being recycled. This was after I went to see how plastic waste — from our homes — was being separated and traded by the poor in our city. "Where does this plastic go?" I had asked in Tikri, located on the outskirts of Delhi. "To Bawana and Narela (industrial areas also in Delhi)," I was told. So, here was I, standing inside one of the many factories that buy this waste and recycle it. Recycling is a big word, but what does it mean?

It goes broadly like this. This waste has to be segregated carefully as each factory can process only one type of plastic. It is first cleaned in vats, then boiled, heated and made to run through coils until it becomes like wire. This plastic wire is shredded into granules of plastic, which is used again to make new products. The people doing this work are poor and the working conditions are pathetic. But they do it for their livelihoods — a trade which makes a resource of our waste. Let's not undermine their effort. If this waste was not so-called processed, it would have been burnt in the open or in poorly constructed landfills. Bawana is why we are not "yet" totally wasted. It is our saviour.

But the economics of this trade work only when the health and environment of the poor are devalued. It was in 1991 when the then chief economist of the World Bank, Larry Summers, had advocated that toxic waste and polluting factories should be moved to least developed countries. Summers, who then went on to become president of Harvard University, was pilloried for this idea by all — but he has the last laugh. This is the business order of the globalised world. It moves polluting factories and mountains of waste into the lands and hands of the poor, all in the name of commerce and livelihoods.

When China finally stopped the import of plastic waste in 2018, new markets had to be found. Many countries, including Malaysia and Indonesia, became the willing dumpyards, till they decided enough was enough. But plastic waste is finding new ports where the costs of recycling would be cheaper and would benefit local business and provide employment. All good. This is the modern world's notion of a circular economy. Summers' version has come true.

It is another matter that these receiving countries are already drowning in their own waste. The fact is that if the rich could pay the real costs of recycling, they would not ship it to poorer countries (I mean the rich of the first world and the rich of our world). The business is about cutting costs. And it is growing. At the May 2019 meeting of the Basel Convention — an international agreement that binds countries to be responsible in their trade of hazardous substances — plastic waste was included for the first time. But not without a fight. The amendment by Norway to regulate trade in certain kinds of plastic was contested strongly by the US; and finally, after much dilution, it was agreed that a distinction would be maintained between contaminated plastic waste and the so-called clean plastic waste, which is destined for recycling in an "environmentally sound manner". So, some control has been brought in, but trade will continue and it will supposedly work for all. The Summers Doctrine again!

The question is whether this is the way ahead. Waste can be a resource. There is no doubt about this. It is also clear that we must recycle and reuse as many times and as much as possible. The Basel Convention may try to stop illegal trade in hazardous substances, but it allows waste to be traded, recycled and processed in a "green" and sustainable way. Given the economics of recycling, that would only mean that this will be done where costs are cheap and health and environment are discounted.

It is not just plastic and it is not just the interests of the rich. While the European Union took a strong stand on plastic waste, it also sought permission to export electronic waste. Then we have second-hand clothes or second-hand cars swamping African nations, all in the name of global charity as the poor can now afford better clothes. This is leading to new forms of local trade interests, which then want to trade in trash. It is their business.

It is time we re-thought this commodity business of waste. It is time we re-worked the "Not-in-my-Backyard" to "In-my-Backyard". Every city must handle its own waste, including its processing. Only then will it become more responsible in its production and recycling. We need to close the circle of this circular economy to make it work. Not Summers-style. But really sustainable-style.

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Travails of a radical patriot

BOOK REVIEW

KEVIN BAKER

"Think of this story as a wheel," David Maraniss writes in an author's note at the beginning of his new book, *A Good American Family*. "The hearing in Room 740 is the hub where all the spokes connect."

Room 740 in Detroit's Federal Building was where Maraniss's father, Elliott, was summoned to appear before the notorious House Un-American Activities Committee (HUAC) one day in 1952, to answer charges that he was a member of the Communist Party. Simply being subpoenaed to appear had already cost Elliott his job, and his refusal to cooperate with the committee's questions would force him into years of desperate struggle to keep his family afloat.

Elliott Maraniss was no atomic spy or government mole. He was a rewrite man at *The Detroit Times*, a World War II vet with a wife and three kids. HUAC had come to Detroit hoping to find communists in the United Auto Workers, a powerful liberal institution; people such as Elliott and his wife's brother, Bob Cummins, were just "collateral damage," expected to make "a few acts of repentance and contrition" — bow their heads and name names of old friends and comrades in the ongoing theatre of the Red scare. If they didn't, they were dismissed after a brief interrogation with their lives in tatters. Elliott was not even permitted to read a prepared statement, though he was allowed to file it with the committee.

Now, David Maraniss, in his "long overdue attempt to understand what had happened to my father and our family and the country during what has come to be known as the McCarthy era," has unearthed that statement, and that moment. A winner of two Pulitzer Prizes in journalism and one of our most talented biographers and historians, Mr Maraniss has used his prodigious research skills to produce a story that leaves one aching with its poignancy, its finely wrought sense of what was lost, both in his home and in our nation.

David's father was "a liberal but undogmatic optimist," whose mantra was "It could be worse." He loved baseball and literature and funny songs; he once wrote a column under the moniker "the Ol' Railbird"; and he had an abiding passion for nearly everything to do with the American heartland. So how does such a man end up writing Soviet propaganda under a fake name for The Michigan Worker? "I can appreciate his motivations, but I am confounded by his reasoning and his choices," Mr Maraniss confesses.

Elliott was the son of Jewish immigrants from Odessa and Latvia, a Boy Scout who grew up in Coney Island, an outstanding student and editor of the school paper at Abraham Lincoln High School — a place almost painful to behold in its glowing idealism and dedication to learning, even in the midst of the Depression.

He also encountered a key influence on his political development: 17-year-old Mary Cummins, a wisp of a girl with strawberry blond hair and deeply held radical convictions. The Cumminses were another remarkable American family, originally dirt-poor Kansas homesteaders living in a one-room dugout cut out of a hillside. Mary's father was a civil engineer who couldn't afford to finish his degree, but made enough money to drive a Cadillac and send his five children to college.

By 1939, as editorial director of *The Michigan Daily*, Elliott was defending the monstrous Stalin-Hitler pact that triggered World War II — a stance that outraged and mystified many of his readers and friends, as well as his son, who calls it one of Elliott's "indefensible positions." When the war reached the United States, Stalin was back on the side of the Allies and both Maranisses threw themselves into the struggle. Elliott enlisted, while Mary helped build B-17s, and advocated for civil rights at her plant.

Rising to the rank of captain, Elliott was put in charge of a black salvage-and-repair company in the still segregated Army, arriving in Okinawa in July 1945, just after the terrible battle there. He excelled in his position, and the experience seemed to fill him with patriotic ardour. He wrote passionately to his wife about Franklin Delano Roosevelt, General MacArthur and especially Dwight Eisenhower, whom he would later admit to having voted for in 1952.

Unbeknown to Elliott, though, his assignment to command black troops was the end result of a desire by military intelligence, wary of his "communistic" tendencies, to exclude him from sensitive work while in the Army. Before his file was finally sealed, some 14 FBI agents would interview 39 "confidential informants" about him. Their investigation would culminate in Room 740, but it would not end there. Even after HUAC had finished with him, the FBI sent agents to interview Elliott's employers whenever he got a job, knowing it would likely cost him the position.

For all of Mr Maraniss's research, a mystery remains at the heart of "A Good American Family": Just what were his parents, and especially his father, doing in the Communist Party in the first place? This is a question Maraniss cannot answer, because his parents, for one reason or another rarely spoke of it. About the furthest his father would go was to admit that he had been "stubborn in his ignorance about the horrors of the Soviet Union." But this gives us little insight into how this great American spirit ended up stuffing himself into a closet of dreary Russian dogma.

In the end, even in the best of families, some things remain secret.

A GOOD AMERICAN FAMILY
The Red Scare and My Father
David Maraniss
Simon & Schuster; $28; 416 pages