Opinion

SATURDAY, AUGUST 10, 2019

ON J&K'S FUTURE

Prime Minister of India, Narendra Modi

J&K will not remain an UT forever. You will get the opportunity to elect your representatives soon. I want to tell the people of Jammu and Kashmir that your representatives will come from among you

Turning vegetarian could help fight global warming

IPCC research shows shows dietary changes could bring emissions down by 8 billion tonnes annually by 2050

IT HAS BEEN clear for sometime that the fight to lower greenhouse gas (GHG) emissions, and mitigate climate-change impact, rests on a drastic rethink of global land use. A large part of land use is tied to human diet, from pastures for grazing of meat animals to agriculture. A new report by the Intergovernmental Panel on Climate Change (IPCC) on climate and land says a plants-based diet will be kinder on the planet than a meat-based one. It recommends that governments, especially those of rich nations, where meat consumption is high, work on reducing this.

Land use and management, including agriculture and deforestation, contribute almost a quarter of the GHG emissions. Unless land is managed more sustainably, keeping global warming under 1.5°C above pre-industrial levels, is impossible—countries, thus, have included land-use, land-use change and forestry in their Intended Nationally Determined Contributions announced as part of the 2015 Paris Agreement. While deforestation for pastures to graze cattle, like in Brazil and Colombia, is particularly emission-intensive, cattle, too, produce large amounts of methane, a potent GHG. Besides, the emission foot-print of manufacturing animal-feed, water- and electricity-use in raising and slaughtering of meat animals, and processing/packaging of meat is significant. The IPCC report, thus, says that balanced diets that are plant-based and feature sustainably-produced animal-sourced food "present major opportunities for adaptation and mitigation". Indeed, by 2050, the report says, dietary changes could free up millions of square kilometres of land and reduce global carbon emissions by upto 8 billion tonnes annually (relative to business-as-usual). Though, perhaps with the politics and socio-cultural sensibilities associated with dietary habits in mind, authors of the report have refrained from telling people what to eat. Given land use across the world contributes $75-85 trillion to the global economy annually (2011, based on the value of the dollar in 2007)—this is many times the world's combined GDP—influencing land use in favour of more sustainable practices is also a fraught economic question, with the livelihoods of hundreds of millions of people tied to it.

The risks a shifting to a largely plant-based diet also must be considered. Rice-farming, for instance, accounts for 24% of agricultural methane emissions. In a country like India, where rice is a staple and one of the largest agricultural exports, pushing a plant-based diet could result in more demand for unsustainably produced rice. Also, nitrous oxide emissions—a potent heat-trapper, with one tonne being equivalent to 265 tonnes of CO2 over 100 years—from agriculture have almost doubled since the 1960s, given fertiliser application has increased nine-fold globally. Besides, research by the Carnegie Mellon University shows that, without reducing caloric intake significantly, simply changing the diet to include the US department of agriculture (USDA) advised food mix, or reducing caloric intake while sticking to the USDA food mix recommended for a healthy weight, will increase GHG emissions and energy/water use.

The window to act on sustainable land use is narrowing fast. Human use already affects 60-85% of forests and 70-90% of other natural ecosystems. Land—the forests on it as well as the soil—plays a key role as a carbon sink. But, with manifest climate change effects, desertification and degradation of land is becoming an ever-growing threat, and humans are responding with even more unsustainable use—fertiliser use, excessive groundwater extraction, stripping down of rainforests, etc, are key examples. The IPCC report, therefore, calls for stepping up efforts to keep the land productive while enhancing its carbon-absorbing capacity—a carefully calibrated, primarily plant-based diet could be one way to do this.

Tackling lynch mobs

Rajasthan has come up with a law, other states must too

RAJASTHAN HAS DONE well to, in response to a Supreme Court recommendation, come up with a special law to deal with lynch mobs. Though the Opposition protested against the "Rajasthan Protection from Lynching Bill, 2019" and argued that existing laws were good enough, this is not quite true; though, while the Opposition argued that some of the Bill's provisions—even two persons can be defined as a mob—could be misused by classifying other crimes as mob violence, this is something that needs to be kept in mind by the investigating authorities. The Bill makes lynching a cognisable, non-bailable and non-compoundable offence, punishable with up to seven years imprisonment and fines of ₹1 lakh if the victim is injured, and this goes up to life imprisonment when the violence results in the victim's death. And, in a bid to deter mob violence, the Bill treats conspiracy, aiding, abetting, and attempt at mob lynching in the same way as it does perpetrators and assailants, and even recognises creation of a hostile environment, distribution of offensive materials, etc, as allied criminal offences. Moreover, the Bill is not only retributive but also rehabilitative, stipulating that victims of mob lynching be compensated by the state government under the Rajasthan Victim Compensation Scheme, and that the state take necessary measures to assist in the rehabilitation of any such victims who might suffer a displacement.

Other states need to take a cue from Rajasthan and come up with similar laws at the earliest. Ideally, as the Uttar Pradesh State Law Commission did last month, when it came up with a draft anti-lynching law, there should also be strict rules for the police and others in authority whose job is to prevent lynching. This includes punishment for not providing protection to the victim if violence was apprehended, failure to act on time, failure to record details of the crime, and so on; if there is no provision to penalise those whose jobs are to prevent such crimes, chances are all laws will come up short. This is a shortcoming in Rajasthan's Bill. Amazingly, though the state's law commission took the initiative on its own, Uttar Pradesh has yet to come up with an anti-lynching law; and this is despite the fact that Uttar Pradesh has recorded 20 distinct incidents of mob violence resulting in 11 deaths since 2015. While the number of those killed/attacked by lynch mobs is likely to be much smaller than those in conventional crimes like murder, the purpose of lynch mobs is to generate fear in certain communities/classes of people; to that extent, the punishments have to be as stringent as possible.

MoreMEDICS

Govt has done well to accept the findings of the WHO report on quacks, the one it had contested earlier

THE GOVERNMENT'S DESPERATION over clearing the air on the National Medical Council (NMC) Bill has forced it to accept and acknowledge a problem that it had, only last year, denied even exists. The NMC Bill talks of bridge course to enable Ayush practitioners to prescribe allopathic medicines—this will take care of the poor doctor-patient ratio that India has. As per a *Times of India* report, while the government, in January last year, had termed "erroneous" the WHO finding that nearly 57% of those practising allopathic medicine in the country didn't have any medical qualification, now, it has included the figure in its FAQs over the NMC Bill. The NMC Bill talks of Community Health Providers—healthcare professionals who can be trained with the bridge courses.

India's doctor-population ratio remains a sickly one doctor for a thousand people. Thus, it is crucial to accept the case for having community health providers. India needs more doctors, and ideas like converting district health hospitals into medical colleges make eminent sense. Until this can be achieved, the country needs to work with what it has. Besides, as Devi Shetty of Narayana Health and Srinath Reddy of Public Health Foundation of India highlight, India's problem is over-medicalisation. Reddy points to the case of mid-level health workers in Chhattisgarh who have proved better than doctors at treating primary care conditions, especially malaria. He emphasises the need to train nurses to become 'nurse practitioners' and 'nurse anaesthetists'. Shetty, on the other hand, says that "even in the litigation-happy US, 67% of anaesthesia is given by nurses, not doctors". If more of community health providers can do the same, it would only help rural health care. More important, it would make more sense to impart the necessary training to a large talent pool of health professionals than let quacks thrive.

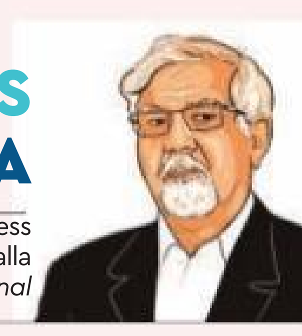
NO PROOF REQUIRED

NO ECONOMY HAS SUSTAINED GDP GROWTH WITH A REAL POLICY RATE ABOVE 1.75%. FOR THE LAST TWO AND A HALF-YEARS, THE REAL POLICY RATE HAS AVERAGED 100 BP HIGHER IN INDIA

Monetary policy: Facts, Opinion, Governance

SURJIT S BHALLA

Contributing editor, Financial Express
Twitter: @surjitbhalla
Views are personal



THIS TIME, MP does not mean Member of Parliament, but Monetary Policy. What I want to discuss today is the FOG surrounding monetary policy in India. It used to be the case, around the world, that a deliberate fog was created around central bank speak. That changed post the 2008 financial crisis. Central banks around the world went for three Cs—Clarity and Consistency in Communication. All advanced country central banks go for the 3Cs; among EMEs, I don't know, but what I hear foreign investors say is that the developing world is much closer to the advanced economies than to India.

Is India as different as claimed by "experts"? My own experience, and interpretation, is that India is very different because the experts (perhaps including those at the Central Bank) look at monetary policy very differently. Most importantly, Indian experts look at the monetary policy through nominal lenses; economics is about the real world. After all, nobody talks about nominal GDP growth; when we discuss growth, it is growth adjusted for inflation. Why don't we do the same with the MP variable called the repo rate—or talk of real borrowing and lending rates?

On August 7, the MPC reduced the repo rate by 35 bps, to 5.4%. The first publication to be off to the races was *Bloomberg Quint* which headlined its story "35 Basis Point Cut Takes RBI Rate To 2010 Level". The story was accurate. In April 2010, the RBI raised the repo rate to 5.25%. CPI inflation at that time was 13.3%, WPI inflation was 10.5%, and the SBI lending rate was 11.8%. IIP was growing at 13%.

It certainly doesn't take a weatherman economist to figure out that the repo rate of 5.4% in August 2019 is not even on the same planet as April 2010, let alone be uttered in the same line. But, I want to quote from some of the editorials after the RBI move. *Business Standard* opined that "the central bank is doing its part by *progressively reducing the cost of money*" (emphasis added). Editorial in *Mint* argued that what the RBI/MPC did was "the best it could have done under the circumstances, grim as they are". It also quoted Governor Das as stating that the committee felt that "25 bp would have been inadequate, while 50 bp would have been excessive". And why didn't RBI undertake a larger cut? The *Mint* view: "Because it did not want to send out a panic signal by easing monetary conditions too much, too fast".

The MPC action (inaction) came against a backdrop of central banks around the world sending out panic signals by cutting lending rates. But to continue with the editorials. The *Financial Express* headlined its editorial "RBI is doing its bit, over to government now". There is elaboration a few lines down. "But the central bank can only do so much. Indeed, it is doing more than its best to create a conducive lending environment for banks". *Economic Times* editorial, "*Slashing* rates by 35 bp, dumping multiples of 25 bps as the quantum of rate change, signals non-routine concern over growth, as also restraint to avert any panic. It also signals RBI's capacity to go beyond convention" (emphasis added).

There is a surprising uniformity (identity?) in the editorials—in addition to the fact that they have got the simple fact of cost of money grotesquely wrong. If I were Governor Das, I would be worried. After every Budget, industry gives a strong heads-up to whatever fiscal policy package the government comes up with. Out of 10, the ranking is always—good, bad and ugly budgets, the same—a robust 9. A lot of us (including the pink newspapers) have criticised this hypocrisy and this "Big Brother is watching" fear. This lack of objective analysis is worrisome. But, why have sheep newspapers not conducted objective analysis of RBI/MPC actions?

What could the editorials have said? They could have pointed out that inflation is phenomenally low, and below the notional 4% target for the *third* successive year. While the nominal repo rate is the same as 2010, the real repo rate is at 2.6% compared to minus 8.1% in April 2010. Stated differently and equivalently, the cost of capital (repo rate) today is nearly 11 percentage points (ppt) *higher*. SBI lent money then at 11.75%—today, the nominal lending rate of SBI is higher (with much lower inflation) by 2 ppt at 13.75%.

> **Every monetary statistic contradicts the expert assessment that monetary policy is reducing the cost of money**

The system is broke, including the experts who report on the system. The same experts blamed the lack of liquidity for the economic slowdown, not the high real rates. Everyone was shouting lack of liquidity as the cause for slow and declining growth in 2018. With this expertly felt lack of liquidity in 2018, industrial production growth Jan-May 2018 averaged 5.4%. With ample liquidity (and all the papers quoted above congratulated RBI for successfully introducing the much needed liquidity in 2019), IIP growth has averaged 1.9% in 2019. The first five months of 2010 IIP growth averaged 11.9%. But wait a minute—weren't we coming out of the 2008 financial crisis and that is why IIP was so high in 2010 and not because of real interest rates? There is partial truth in that.

Compare first five months of 2011 with 2019. Industrial production growth: then 6.8%; today 1.6%. Real repo rate: then minus 2.8%; today plus 3.4%. Real SBI lending rate: then 3.6%; today 11%. Liquidity: then ample; liquidity today, ample.

Das took over as RBI Governor in December 2018. He has been in office for only eight months and it is unfair to assess performance over such a short time period. Nevertheless, few facts are relevant. Eight months prior to Das's arrival, inflation had averaged 3.9%, repo rate averaged 6.3% and the real repo rate averaged 2.4%. Over the last eight (Das) months, (till July 2019), inflation has averaged 110 bp lower 2.8%; the repo rate has averaged 20 bp lower at 6.1%, and the real repo rate 90 bp higher. Liquidity is very stressed in 2018 (according to many experts, that was *the* cause for the slowdown) and very ample in 2019.

Every monetary statistic contradicts the expert assessment that monetary policy is reducing the cost of money. It is simple math really—if inflation goes up by 10%, and my cost of borrowing goes up by 5%, the cost of money has come down. And just the opposite when inflation declines more than the repo rate. Why is this simple math *seemingly* not understood by experts?

There are additional factors constraining growth in 2019 and beyond. Tariff wars have intensified, world growth has slowed down, and our competitors are lowering real rates and lowering tax rates. We are raising both. The expert media fully recognises (most of them do) that higher tax rates in a slowing economy will slow GDP growth even more. But, why this arrogant dismissal of the one factor the rest of 180 countries find the most potent cyclical, and structural factor, to enhance growth? More than a decade ago, Deputy Governor Rakesh Mohan opined that lazy banking was an important and unique aspect of Indian banking. But, why do experts endorse lazy banking as a solution to our growth problems?

Household savings in India

Policy environment for savings in India is sub-optimal. This is particularly true of the household sector, which has been the largest contributor to overall national savings

NIRVIKAR SINGH

Professor of Economics, University of California, Santa Cruz
Views are personal

INDIA HAS TWO fundamental problems in its pursuit of higher economic growth. First, it needs to increase investment. Second, it needs to increase savings. Both investment and savings have fallen as percentages of GDP, and are below the levels needed to support GDP growth of 8-10% a year. There is a counter argument that higher growth itself will rekindle animal spirits of investors, but I think the starting point has to be with creating prospects for better investment returns. The investment slowdown is related to the collapse of the preceding investment boom, which included too much corruption and, more generally, misallocation of capital. Until the overhang of bad assets is cleaned up, so that credit flows more freely again, investment will stagnate. The government has been trying, but perhaps not hard enough. The battles with RBI on this front have also not helped. Efforts to attract foreign investors will also not achieve too much until the financial sector and corporate balance sheets are cleaned up. Even then, the policy framework for investment has to improve, in terms of taxation, infrastructure, and stability.

The savings side is trickier, but also has the potential for plucking some low hanging fruit, with the right degree of policy attention. This is because the policy environment for savings in India is sub-optimal. This is particularly true of the household sector (including smaller firms in the Indian case), which has been the largest contributor to overall national savings. The other sources of savings—corporations, government and foreigners, are potentially important, but their determinants are more complicated, including whatever factors determine the investment climate, and the politics of government expenditure. Households, however, can be potentially reliable sources of savings.

There are three interrelated aspects of household saving where policies can be changed to make a difference. First, the level of household savings has fallen in recent years, despite high real (though not nominal) interest rates. Second, Indian households tend to put a relatively smaller proportion of their savings in financial assets, versus physical assets such as gold and real estate. Third, Indian households put relatively little of their financial savings into long term savings such as pensions and insurance products, versus bank accounts. All three factors result in a paucity of funds that can be intermediated into productive investment.

Tarun Ramadorai, who headed the RBI committee on household savings that reported in 2017, has pointed out that the tax incentives for long term savings through pensions are muddled and weak. He has made detailed proposals for clarity and simplicity in the design of pension schemes and the tax incentives that accompany them. This is about more than just "nudges," and requires significant, but straightforward, policy changes. The government may be worried about possible losses of revenue through tax breaks, but this seems to be an area where the returns will justify any short term revenue hit.

Last year, Radhika Pandey, Ila Patnaik and Renuka Sane, in the India Policy Forum, provided a detailed empirical analysis of the impact of tax breaks on household financial savings, and found that such incentives must be carefully designed to avoid distortions between different types of financial saving. They also emphasised the need for more sensible regulations, giving insurance companies and pension funds more room to invest in assets other than government bonds. In brief, household savings have to be channelled efficiently to more productive investments.

The need for better channelling of household savings is driven home by a more recent analysis by Patnaik and Pandey, in an NIPFP working paper. Government policy on this front does not seem to be coherent or sufficiently evidence-based. Budget proposals often seem to be piecemeal and fragmented. Nevertheless, one can characterise this area as low-hanging fruit, because there is so much room for improvement. Despite the nuances of having different types of financial saving, with different types of institutions and regulations for collecting and channelling them, the underlying economic behaviours are not difficult to model and analyse.

A comprehensive, evidence-based policy approach to household financial savings will also help draw attention to institutional weaknesses in financial services and financial intermediation. It can be politically difficult to deal with such weaknesses without an overarching goal. Improving the level, composition and channelling of India's household saving can provide the requisite framing for political feasibility of more fundamental institutional reforms, as well as reforms in tax policy and regulation for the financial sector. Institutional reforms here could include a greater role for private sector firms, more competition, and more effective use of digital technology. Patnaik and Pandey make all these points, and they just need more detailed modelling and simulation for evaluating policy options.

None of the above makes redundant the need for continued improvements in the climate for non-financial firms to do business, or to innovate, or to export. All the real aspects of producing and selling things in India are subject to hurdles that the government has the power to reduce or remove, if it decides it wants to be growth-promoting rather than rent-seeking or populist in its policy stance. But higher growth requires higher investment, and that will need more household financial saving, channelled to productive uses. This is an area that needs better policy attention than it has received.

LETTERS TO THE EDITOR

PM Modi's address

PM Narendra Modi's post-Article 370 abrogation TV address to the nation has come in for fulsome praises from many people, including the media, for reaching out to Kashmiris with a slew of promises. But, the moot question is whether his promises of early polls, restoration of statehood, benefits to government employees on par with their counterparts in UTs, filling government job vacancies and investment will make up to the people of Kashmir for what they were robbed off—special status. At best they are a balm inefficacious in healing the deep wound to the Kashmiri psyche. People do not trade their identity for favours. Winning the hearts and minds of Kashmiris alone will facilitate their integration into India. The withdrawal of special status and privileges is not the way to win their *vishwas* (trust). As for the promise of development, human development indices in Kashmir are relatively better than in most parts of India. We are also struck by the incongruity of a leader of a party that never tires of accusing the secular parties of 'Muslim appeasement'. PM Modi did not speak a word on the deployment of more troops and the house arrest of Valley's mainstream leaders. Why leaders like Ghulam Nabi Azad and Sitaram Yechury are prevented from visiting the people of the Valley while NSA Ajit Doval is featured interacting with the local residents defies understanding. If what is going on in the name of Hindu revivalism in the rest of the country, the reading down of Article 370 may well be a move to superimpose Hindutva culture onto Kashmir's indigenous culture or *Kashmiriyat*. The hailing of the annulment of special status as the 'correction of a historical wrong' by *Hindutvawadis* says it all!

— G David Milton, Maruthancode

●Write to us at feletters@expressindia.com

R.N.I. Reg. No. 6188/61 Printed for the proprietors, The Indian Express (P) Ltd by Vaidehi Chintaman Thakar at The Indian Express (P) Ltd Press, Plot No. EL-208, TTC Industrial Area, Mahape, Navi Mumbai-400 710 and published from Express Towers, Nariman Point, Mumbai-400 021. Editorial & Administrative Offices: Express Towers, Nariman Point, Mumbai-400 021. Phone: 22022627/67440000. Fax: 022-22856323.
Chairman of the Board: Viveck Goenka, Managing Editor: Sunil Jain, Deputy Managing Editor: Shobhana Subramanian* (*Responsible for selection of news under the PRB Act)

JAPAN-KOREA TRADE DISPUTE

Japan seeks to emerge from the shadow of history

The biggest trade war of recent times, the US-China dispute, is tied to forced technology transfer and intellectual property rights. But the Japan-South Korea dispute appears tied to Japan's long and arduous struggle to emerge from the pages of history

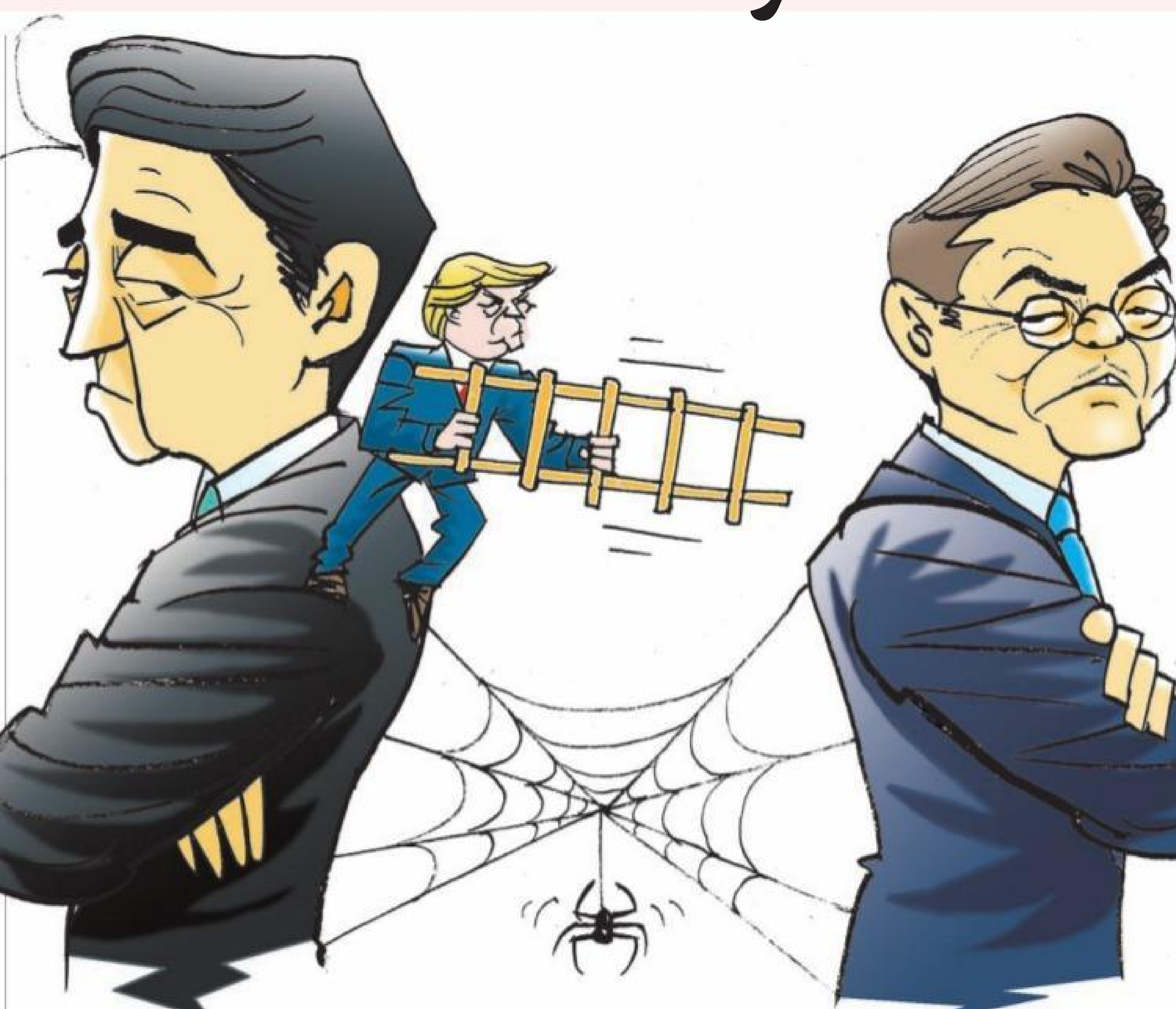


ILLUSTRATION: ROHNIT PHORE

ANURAG VISWANATH

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

JAPAN, THE QUIET sentinel of Asia, lives in the future and yet cannot quite extricate itself from the past—caught in the net of history whilst seeking to escape it. Prime Minister Shinzo Abe's attempts to amend the Constitution and the current trade skirmish between Japan and South Korea can be traced back to history—a history that Japan seeks to put behind, but so far with little success.

In fact, Japan's new era, the Reiwa era (literally, beautiful harmony), began May 2019 with the abdication of the Chrysanthemum Throne by Emperor Akihito. The abdication marked the end of the three decades of the Heisei era (peace everywhere). With the Tokyo Olympics 2020 scheduled next year, there is much optimism in the air—an understanding that it will repeat for Japan what Tokyo Olympics 1964 did, which boosted its economic renaissance.

Japan's aspirations reflect in the winds of its domestic politics under the 64-year-old Abe, now in his seventh year of office. In fact, the years of political instability seem to have passed. If Abe stays in office until November 2019 (which is a certainty), he will surpass 2,886 days in office (tolled by PM Taro Katsura in the early 20th century) and become Japan's longest-serving PM in history. Some achievements, as Abe articulated at Davos 2019, are growth in Japanese GDP by 10.9% (in his six years of office), female labour participation hitting 67% and an ageing population (above 65) accessing job opportunities. But observers such as political scientist Lully Miura say that Abe continues to be in power because of "an exceptional combination of specific conditions," including his foreign policy and the administration managing its public image carefully.

But it is Abe who has sought to turn a page in Japan's constitutional history, seeking an amendment for the first time in its 72-year history. Japan's surrender in the Second World War led to a postwar pacifist Constitution. Despite being a formidable power in its own right, Japan is dependent on the US for defence—it is bound to the US by a defence treaty (1951, revised in 1960) where the US has military bases in Japan in exchange of protecting Japan in case of an attack. Abe and his allies have sought a revision of the Constitution, seeking the formalisation of Japan's de facto military, Self-Defense Forces (SDF), which would entail parting with the Article 9 (no-war clause) of the Constitution. Article 9 says that "land, sea and air forces, as well as other war potential will never be maintained."

The recent July elections to the upper house of Parliament (House of Councillors) impacted amendment. Of the 124 seats, Abe's Liberal Democratic Party (LDP) and Komeito won 71 seats (57+14), and the Constitutional Democratic Party (CDP) 53 seats in the 245-member house. The parties in favour of amending the Constitution, the LDP and allies Nippon Ishin no Kai (Japan Innovation Party) and Komeito (total of 157 seats), fell short of the two-third 'super-majority' (164 seats) needed to initiate the amendment. A day after the elections, Abe sought to keep the issue alive by discussing it. He now seeks amendment in 2020. The issue of Japan remilitarisation continues to be alive.

The public increasingly believes that Japan is vulnerable, ineffectual and impotent as a balance to a rising China, which boasts considerable military prowess.

History is also at play in Japan-South Korea relations, both staunch US allies, but who cannot see eye to eye. Japan and South Korea have several common concerns, including the security dilemma in the Northeast peninsula (North Korea and China), but a trilateral (US-Japan-South Korea) has not been forthcoming.

> Relations between the two are rocky because of 'historical animosity' that dates back to the Japanese colonisation of the Korean peninsula (1910-45)

Relations between the two are rocky because of 'historical animosity' that dates back to Japanese colonisation of the peninsula (1910-45). In fact, the recent move by Japan to strike South Korea off its 'white list' (of 27 preferential trade partners) effective August 28 is not because of a trade dispute per se, but because of history.

The dispute sparked when the South Korean Supreme Court ruled that Japanese companies Nippon Steel, Mitsubishi Heavy Industries and Nachi Fujikoshi compensate wartime forced labour. Japan views this as flogging the acrimonious past. As Japan views it, this was resolved in 1965 when relations were normalised, and in terms of reparations, Japan paid $2.4 billion by way of loans and aid to Korea.

But the issue of forced wartime Korean labour in mines and factories, the forced prostitution of Korean women to provide sexual services to the Japanese army—'comfort women'—and the plight of the Koreans who continue to stay in Japan (regarded as second-class citizens) has haunted bilateral ties. In 2015, President Park Geun-hye inked what Japan called a deal to "finally and irreversibly" settle the issue of 'comfort women' through a $9-million deal, which many viewed as a pittance. In 2018, the foundation that Japan funded to support and provide funds to the 'comfort women' was dissolved.

Japan was alarmed with the decision of the South Korean court to order the seizure of Japanese assets, which it viewed as damaging Japanese trade and investment in South Korea. Citing 'national security grounds' of 'declining trust' between the two, Japan slapped exports to South Korea with restrictions. Japan has targeted three chemicals (hydrogen fluoride, fluorinated polyimide and photoresists) used by South Korean companies in smartphone displays and chips. This will disrupt the supply chain of South Korea's semiconductor, display (electronics) and automobile industry, and companies such as Samsung, SK Hynix and LG will be affected. Japanese exports to South Korea now need case-by-case approval.

South Korea has responded with strong public opinion and visible nationalist outrage, and has accused Japan of 'weaponising trade'. South Korean customers are boycotting Japanese products in the supermarkets, and South Korea wants to stop military-intelligence sharing with Japan, which has implications on the security of the peninsula. But Japan is unrelenting.

The issue shows no immediate signs of abating, with the US unable to resolve the acrimony of the past. While the US will eventually step in and resolve the posturing, for South Korea, with legislative elections in April 2020 round the corner, backing down may indicate 'loss of face'. The biggest trade dispute of recent times, the US-China dispute, is tied to forced technology transfer and intellectual property rights. But for Asia's quiet sentinel Japan—be it constitutional amendment or trade dispute with South Korea—both are tied to its long and arduous struggle to emerge from the pages of history. The US and now Japan are cases in point of the new dynamics in international relations, where economics is a powerful instrument of political arm-twisting, and so is history.

DATA DRIVE

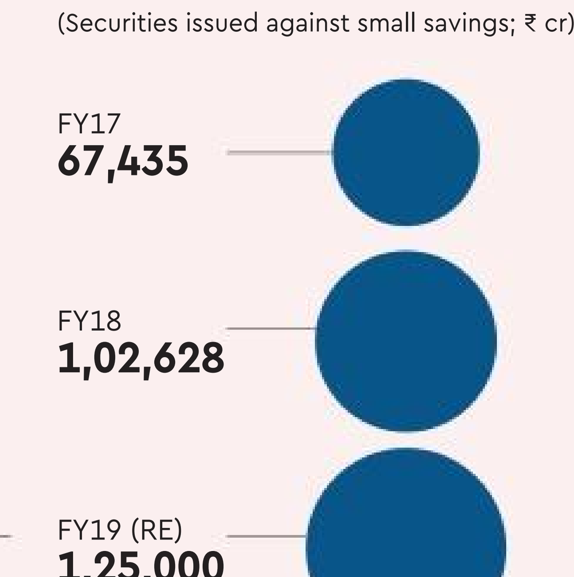
Poor transmission

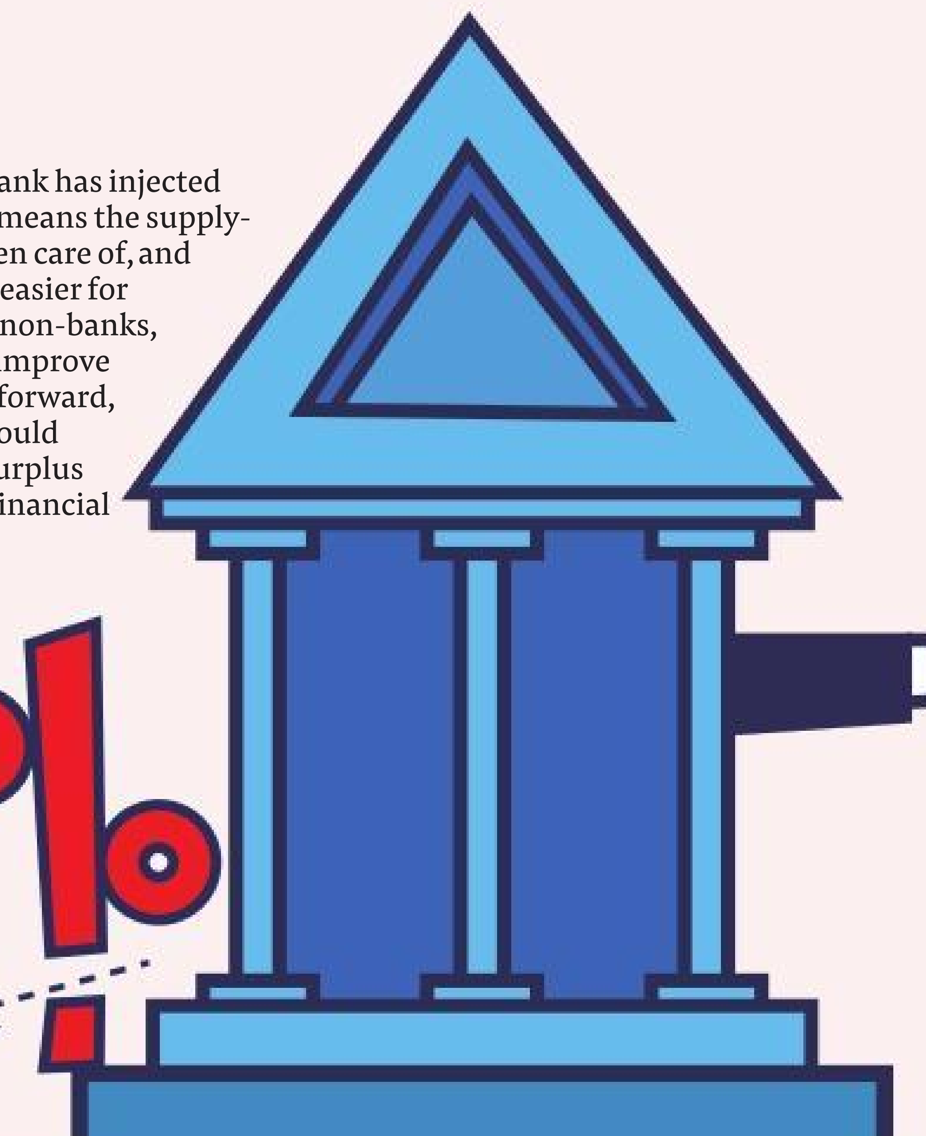
WHILE THE RESERVE BANK of India has cut the repo rate by 35 basis points—the first cut of this magnitude—to 5.4% (the repo rate is now at a nine-year low), the onus is now on banks to cut their lending rates to spur economic activity. In response to the policy, the country's largest lender, the State Bank of India, has reduced the Marginal Cost of Funds based Lending Rate (MCLR) across all tenors by 15 basis points.

Banks have been very slow in passing on the benefits of the central bank's rate cuts to their customers. To be sure, before Wednesday's rate cut, the central bank had cut the repo rate by 75 basis points this year between February and June. However, the transmission of policy rate cuts on fresh loans of banks was only 29bps. The earlier RBI announcement to benchmark new floating rate loans to the external benchmarks appears to have been taken off the table.

Banks have not been able to reduce their lending because of slowing growth in deposits. As a result, deposit rates have remained flattish as banks have found it challenging to pass through rate-cuts, and small savings—given they are still offering much higher rates than bank deposits—are cornering growing shares of the deposit pie. For example, while the five-year deposits rate of the SBI is 6.5%, the five-year post office term deposits fetch 7.7% and Public Provident Fund is fetching returns of 7.9%.

The central bank has injected liquidity, which means the supply-side is being taken care of, and has also made it easier for banks to lend to non-banks, and this should improve liquidity. Going forward, transmission should improve given surplus liquidity in the financial system.





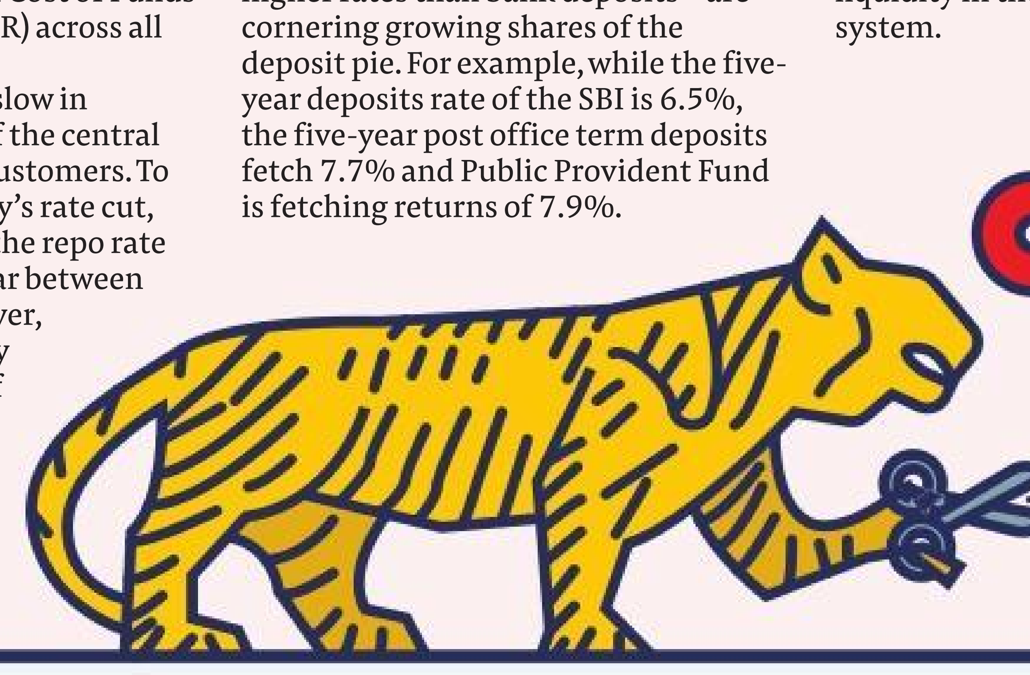
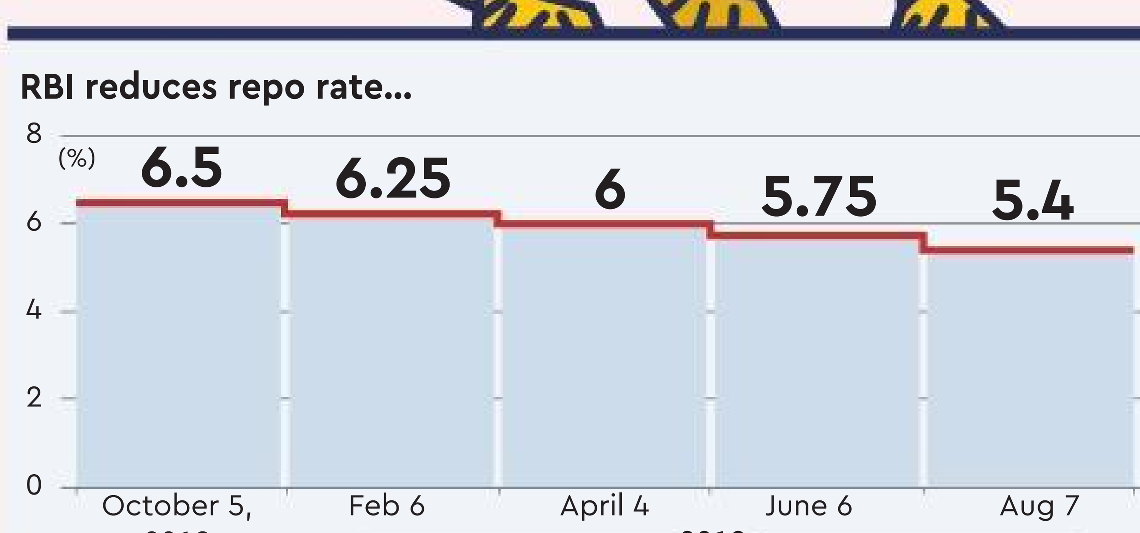
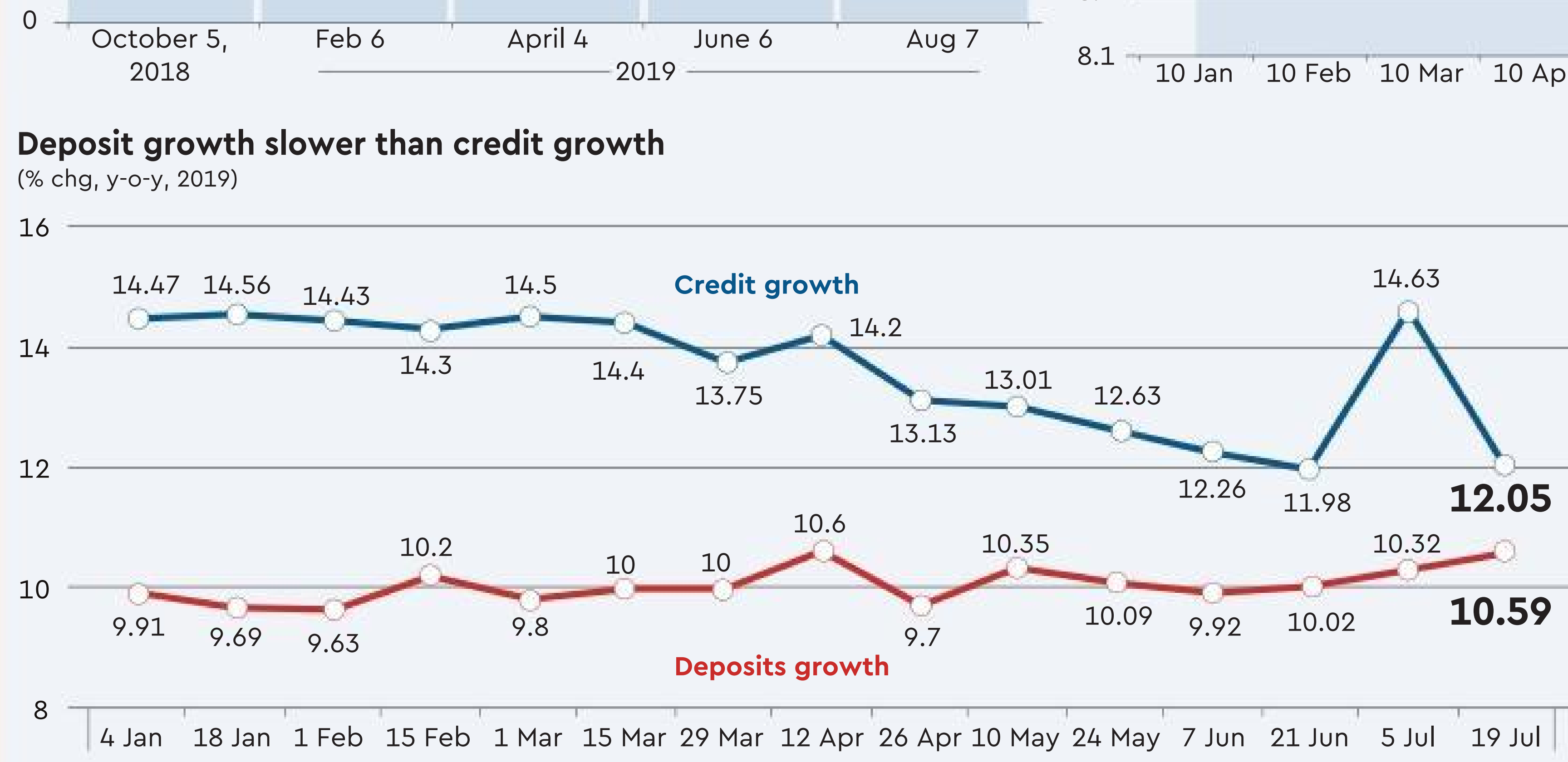
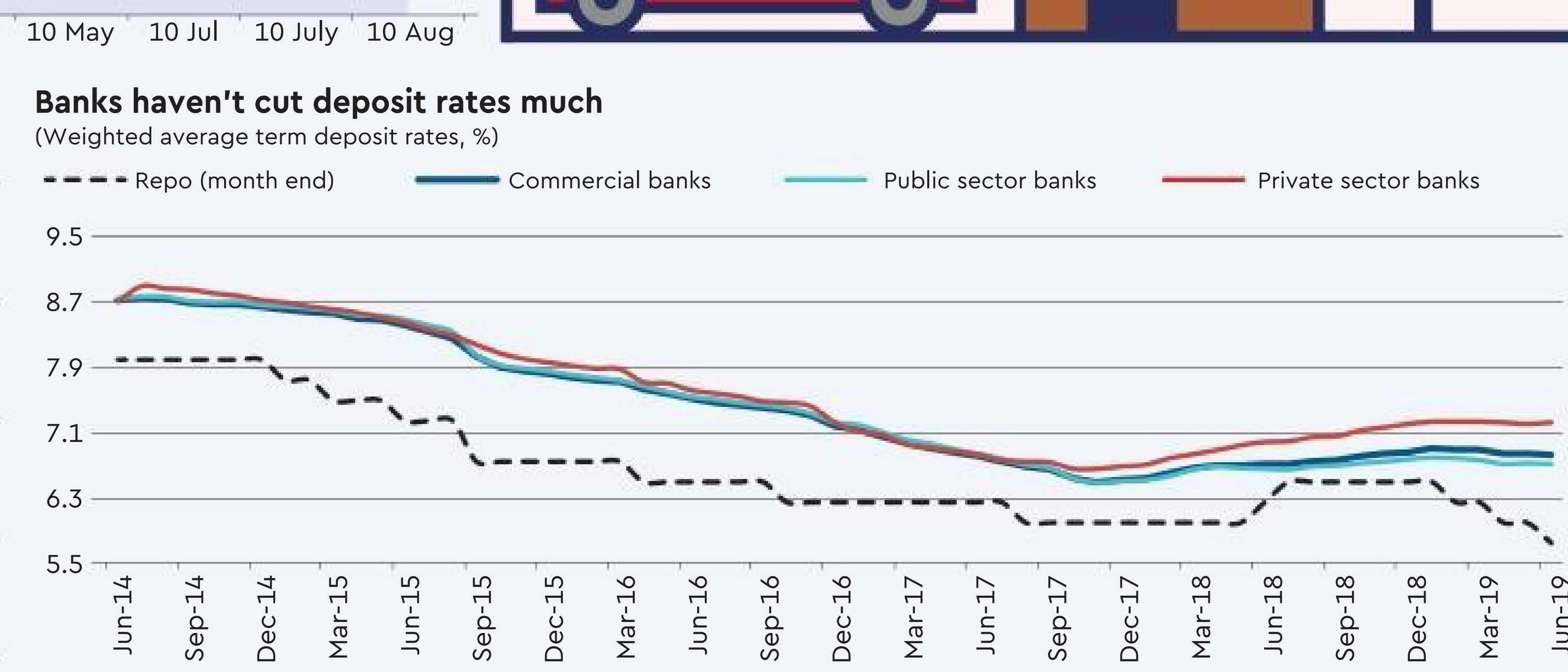


ILLUSTRATION: SHYAM KUMAR PRASAD







Source: RBI, SBI, Budget documents