Opinion

MONDAY, AUGUST 26, 2019

ON CLIMATE CHANGE

Chancellor of Germany, Angela Merkel

From the shift in mobility patterns to the issue of energy generation, I believe we face common challenges. Humankind must treat nature with care and show some humility

Linking social media to Aadhaar is serious overkill

The impact will be to curb even the slightest criticism of govt; nothing could be unhealthier in a democracy

A THE HEIGHT of the anti-Aadhaar movement, the government was at pains to explain that Aadhaar did not infringe on anyone's privacy in any way. By way of example, if a bank account was linked with Aadhaar, all details of bank transactions remained only with the bank—as they did in the pre-Aadhaar days—and did not ever get reflected in the Aadhaar database. Similarly, while a phone number could be linked to Aadhaar, all call details remain with the mobile phone provider; income tax details remain with the taxman, etc. While that may have won the day for Aadhaar, if the proposal to link Aadhaar with social media accounts fructifies, it will bring back the privacy debate and, this time around, it will be difficult to argue that Aadhaar is not a breach of privacy. For, with each social media firm having a list of Aadhaar numbers, it will be very easy to create a profile of people based on their Aadhaar numbers and, more important, even the smallest criticism of the government will be traced back to the person; that's a chilling thought, especially in a country that prides itself on being a democracy. Can you think of an Arab Spring or a Hong Kong-type protest in a country where the government can track even your social media posts?

The government, it is true, doesn't want to have the detail of everyone's Aadhaar-linked-social-media accounts. It only wants them in certain cases. If, say, a video is circulated on WhatsApp that causes tension in Kashmir, the government wants to be able to track down the user; the assumption here is that the phone number used for WhatsApp was probably procured using a fake ID. If not, the government, in any case, can find out the name of the sender; this assumes WhatsApp will tell the government who sent the initial video, and that is the subject of another discussion. But, the short point is that since the numbers of those fomenting trouble by using social media as a force multiplier—the message can never go viral as fast as on social media—is a tiny fraction of the overall population, the greater good lies in not stifling free comment.

In which case, how is the government to trace those trying to create trouble using social media? It will have to be done the old way, with the government asking Twitter/Facebook to block accounts that are seen to be putting out false news/propaganda. In the case of a WhatsApp, assuming the platform doesn't divulge where a message came from, it will have to track messages from phone to phone; it will also be a good idea to tighten norms to ensure only genuine documents are used to buy mobile phones. Good intelligence operations should be able to track when fake news is being peddled on a large scale, and the government should have its own version of HoaxSlayer—staffed with smart people using the best of AI and other tools—to be able to call out fake news; the same social media that works for troublemakers then needs to be used by the government as a force multiplier. The dangers of linking social media accounts to Aadhaar far outweigh the possible gains; hopefully, both the government and the courts that will be ruling on this will realise that.

Sowing trouble

CACP's proposed price-deficiency scheme is a bad idea

THE COMMISSION FOR Agricultural Costs and Prices (CACP), in recommending a price deficiency payment scheme (PDPS) for commercial crops like oilseeds, cotton, maize, etc that have "no assured/established mechanism for liquidation of stocks"—public procurement at MSP, that is—seems to have learned little from Madhya Pradesh's Bhavantar Bhugtan Yojana fiasco. The state had to bin the Bhavantar scheme because it was quite prone to gaming. Indeed, given how few *mandis* are competitive, traders, once they got to know that they stand to benefit from lower *mandi* prices, cartelised to push it down to increase the differential with the MSP, in *kharif* 2017. Farmers, it is alleged, were willing participants for a cut. Madhya Pradesh, where the prices are already generally lower than other states, simply couldn't afford to pay the MSP-differential that cartelised *mandis* managed to create. To be sure, the CACP proposes that the modal/floor price after which the scheme kicks in, be fixed on the basis of price trends over the last four-five years with strict adherence to fair average quality. In addition, it recommends that farmers be encouraged to hold on to their produce in accredited warehouses and be provided loans against warehouse receipts to avoid the typically-low prices at harvest-time. Such farmers will also get PDPS benefits if the market price at the time they choose to sell is below the MSP. These measures may seem like a safeguard against the Bhavantar loopholes, but are hardly so. Indeed, *mandi* cartelisation to game the scheme may be easier at harvest-time, but can't be ruled out entirely at the time farmers want to offload stocks. As for the average price-check, *mandi* cartelisation, again, will be a hurdle, since if traders are unwilling to pick up the stock at a price approaching the floor price, farmers are stuck. Not only will they have to sell the produce at a low price, but will not be able to benefit from PDPS because the selling price doesn't meet the floor price criterion! Indeed, if the government intends to ensure that such cartelisation doesn't derail its PDPS, it will have to keep a check on every single *mandi* in the country.

A much better way to support farmers will be to offer direct cash support for costs, instead of one based on prices. Telangana's Rhythu Bandhu and Odisha's Kaalia are both good examples of this. According to Icrier professor Ashok Gulati, a ₹10,000/hectare cash subvention will cost ₹1.97 lakh crore across the country. If subsidies given to farmers by the states are subsumed, this cost could fall. But, even if the subsidies continue, this amount isn't very different from what the government would likely incur as the cost of a price-support scheme. This will benefit farmers without distorting farm practices and the chances of traders manipulating the scheme, at the cost of both, the farmer and the consumer, are eliminated. Given how the per-acre cost support doesn't interfere with the market, it doesn't affect the competitiveness of India's agri-exports while remaining WTO-compliant. Indeed, if the government were to liberalise agri-exports while moving to a cost-support scheme for the farm sector, farmers will benefit far more than from a price-support scheme prone to rigging.

Smoke&MIRRORS

The Centre's proposed policy on vaping is in contrast to its policy on cigarette/*beedi* smoking

WHILE A UK government health agency has been advising people to substitute cigarettes with vaping, the Indian government is mulling a law to ban the latter. Public Health England—an executive agency under the Department of Health and Social Care in the United Kingdom—maintains that vaping is 95% less harmful than smoking cigarettes. But the Indian health ministry has proposed a ban on the vaping and e-cigarettes. To be sure, many Indian states already have such a ban in place. But, there is no central law banning e-cigarettes and vapes. The proposed ban would entail a three-year jail term and a ₹5 lakh fine for repeat offenders, and comes at a time when industry majors like Juul Labs and Philip Morris International were thinking about expanding their e-cigarette and vape markets in India. At the same time, there is no proposal to ban cigarettes/*beedis* and chewing tobacco.

Although the ministry and the states have cited health concerns for banning e-cigarettes, the problem is the government's unbalanced approach to the tobacco industry. For one, e-cigarettes have been an expensive proposition—cheapest ones cost ₹500, with pods or liquids costing more—were only expected to replace cigarettes. More important, India's tobacco problem is largely *beedi*-linked. While successive governments keep hiking cigarette duties—they pay an excise duty of around 50% right now—*beedis* get taxed at around 2-3%, and chewing tobacco pays around 5-6%. Moreover, while VAT rates differ from state to state, they are roughly 26% for cigarettes and 8-10% for *beedis* and chewing tobacco. As a result, as share of cigarettes halved from around 20% since the 1980s, there has been little drop in overall tobacco consumption. Given that the tobacco industry pays taxes to the tune of 2% of central tax revenues, and employs 7 million people, vapes are certainly not the issue if the government wishes to control addiction.

TAX TRAUMA

RECENT NOTICES ASK START-UPS TO JUSTIFY FAIR MARKET VALUE OF THE SECURITIES WITHOUT MENTIONING SECTION 56(2)(VIIB)—ANGEL TAX HAS SIMPLY MUTATED TO A MORE PERNICIOUS FORM

Angel tax: Not dead, merely deferred

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Views are personal

NEVER HAS A tax displayed the flagrant disconnect between the bureaucracy and business like the angel tax does. In the measures to boost the Indian economy announced by the finance minister last week, angel tax found an explicit mention, causing entrepreneurs to rejoice that this ordeal is over. But the devil lies in the details, and the angel tax isn't dead—it is simply deferred.

Angel tax, or section 56(2)(viib) of the Income Tax Act, 1961, was an insertion by the UPA regime in 2012 as a means of checking the circulation of unaccounted funds through investments into private companies. It sought to attack "high share premium"—a supposed smoking gun of money laundering; instead, it turned out to be a red herring. A high share premium is the consequence of the mathematics underpinning valuation. Simple, legitimate corporate actions like having a small initial capital base and having a low face-value (both mainstays of any technology start-up) can translate into high share premiums. It is no more an indication of money laundering than having high-speed internet is an indication of online piracy.

The reason for this link between high share premium and money laundering arose from details uncovered by the Enforcement Directorate against Jaganmohan Reddy, where it was discovered that people had "paid bribe to Reddy in the form of investments at exorbitant premiums in his various companies to the tune of ₹779.50 crore, apart from making payment of ₹57 crore to him in the guise of secondary purchase of shares and donation of ₹7 crore to YSR Foundation". It was from here that the indelible link between share premium and unaccounted money was cemented in the minds of the tax officers.

The unintended consequence of this 2012 legislation was that it became a tool of harassment of start-ups in the hands of the taxmen. Indian start-ups raise between $12-14 billion of capital every year, with only under 10% of it coming from domestic sources. The bulk of domestic funding comes at the "angel" or "seed" stage—where the risks are the highest. All of them are valued by investors based on their potential and projections, not their present. Due to the factors mentioned above, all these securities were issued at a premium. It is this premium—this mathematical outcome that the taxmen attacked with vigour, raising demands of 30% of the share premium raised by the start-ups. It is no secret that these start-ups were easy pickings for taxmen, who were under pressure to meet collection targets.

Worse, it targets the money from Indian investors alone; no other country in the world has so actively discriminated against its own citizens in their own country. Not even the British would have inserted such a provision in the pre-Independence era.

Over time, with the concerted effort of the media, entrepreneurs, business leaders, DPIIT and the politicians, the tax department drip-fed circulars to address parts of this issue—tilting at windmills instead of tackling the bull by the horns. But in February 2019, there was finally a breakthrough wherein this scourge of angel tax could finally be put to rest. The circular stated that all start-ups would be exempt from the tax provided they don't make any investments into a negative list for seven years from the date of issuing shares at a premium. It is within this list that the Achilles heel of the angel tax exemption lies.

The negative list includes land, building, motor vehicle, aircraft, yacht, jewellery held by then, other than in the ordinary course of business. All reasonable asks as those are assets that do not contribute to general business, and if it does, it is permitted. But, it is pertinent to note that this carve-out in the ordinary course of business doesn't apply to three areas: loans and advances, shares and securities and capital contributions—and therein, as the bard wrote, lies the rub.

Loans and advances: Loans and advances are such an integral part of a business that the format of financial statements mandated by the Company's Act gives detailed instructions on its presentation in a balance sheet. Some of the constituents include security deposits like rental deposits, downpayment on assets, advances to vendors, salary advances, loans to employees for purchasing ESOPs, salary advances and even advance tax.

None of these by themselves are indicative of money laundering and all these are legal under all laws except the angel-tax exemption. What is more surprising is that discharging one's advance tax liabilities can potentially deny the start-up angel tax exemption! A more ironic example of cutting the nose to spite the face is yet to be found.

> The February 2019 circular should be amended to state that loans and advances in the ordinary course of business should be allowed, provided the PAN of the recipient is given

Investments in shares, securities or making capital contribution: On the face of it, one can question why a startup would need to deal with shares and securities at such an early stage, a reasonable ask since the money raised can be invested into other entities, thus perpetuating the laundering of cash. But what the authorities fail to realise is that this hampers business productivity since it effectively bans all joint ventures, subsidiaries, stock mergers and acquisitions and treasury management! No longer can a company expand by setting up subsidiaries in other geographies or joint-ventures with other businesses. Stock M&A, which forms the bulk of consolidation in various sectors, is effectively killed since this would transgress the exemption. Treasury management, wherein companies park excess funds in short-term money-market listed instruments regulated by SEBI, is now taboo.

The most pernicious part of this list is that it this moratorium should continue for seven years after the year in which shares were issued for a premium. So, the argument proffered that a young start-up has no business engaging in such investments is myopic. In the guise of an exemption, the circular places a glass ceiling on growth and ordinary corporate activities. The choice for Indian entrepreneurs is now to either raise domestic capital but sacrifice competitiveness or raise only foreign capital and be exempt from these restrictions. The message from the tax department seems to be that one can start up in India, make in India, too, but if you're Indian, please don't invest in India.

For those who may label this as alarmist, there are already situations faced by entrepreneurs wherein the assessing officers are questioning the exemption on the basis of these weak links. Worse off, the new Finance Act inserted a penalty of 200% of the premium in case a start-up has its exemption revoked. Recent notices received by entrepreneurs as early as last month are asking start-ups to justify the fair market value of the securities without mentioning Section 56(2)(viib)—a clear indication that this issue hasn't died down, it has simply mutated to a more pernicious form. Even the recent notifications state that any tax officer can only open up proceedings on "Angel Tax" with the prior permission of their superior officer isn't relief, it is bureaucracy with extra steps.

If the intention is to bring relief, then the February 2019 circular should be amended to state that loans and advances in the ordinary course of business should be allowed provided the PAN of the recipient is provided. On the issue of investing in shares and securities, if it's made into SEBI registered entities, then it should be allowed. Furthermore, any subsidiary or joint-venture should be precluded from investing in land, jewellery, buildings, etc—thus, plugging the gap that allows the start-up to be used as a via media to make banned investments.

The finance minister spoke about angel tax in the budget—the first time it was mentioned by name in any budget speech since 2012—and stated that it has been dropped for registered start-ups. But unless these issues are resolved, this is a time-bomb waiting to explode. The devil is always in the details, not in the headlines—and the angels are nowhere to be found.

Ushering in a new era of capital raising

Differential voting rights allow for more Silicon Valley inspired investment structuring and negotiations, and could have avoided the debacle of a public Indigo fallout or Mindtree's hostile takeover

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Views are personal

WHAT DO FACEBOOK, Google and Snapchat have in common, apart from being some of the most powerful companies in the world? Unequal voting rights! Yes, at a time when the blue-eyed boy of the Indian startup ecosystem, Ritesh Agarwal of Oyo Rooms, had to devise a leverage-backed buyback in his unicorn to maintain shareholding befitting his founder status, world over, the likes of Mark Zuckerberg and Larry Page have had their voting rights safely secured, regardless of dilutions to their equity stakes through series and series of equity fundraising.

Disproportionate voting rights, known in the Indian legal regime as shares carrying differential voting rights (DVRs), have been a subject of constant policy changes, but with SEBI waking up to smell the coffee recently, when it released the framework for listing of superior rights shares for tech-based startups, it was only time that the Ministry of Corporate Affairs (MCA) followed suit. Some of the laudable changes introduced by the MCA, via amendments to the share capital and debenture rules, include ability to issue up to 74% DVRs (from the erstwhile 26% sanction) and doing away with the notorious regulation mandating a track record of three years distributable profits, which was completely impractical to begin with (for the record, We Work, the $47 billion co-working company, which has been in the news recently over its IPO filing, is still not profit making!).

Let's for a moment assume that Mindtree, prior to its listing, had created a Class B share, with voting rights 10x the voting rights of an ordinary share or a Class A share. The L&T hostile takeover would surely have been a tougher battle to fight, and perhaps the Mindtree founders would still be on the board. In much the same way, the recent public spat in Indigo, between its co-founders, too, could have been preempted if either one of the founders would have secured with himself a special kind of security that gave him larger voting rights. In a larger context, logjams in decision making of a company are mostly the nemesis of 'business as usual', and with prime minister Modi recently branding Indian entrepreneurs as 'Growth Ambassadors', I suppose the brief with the cabinet is clear—make company law easier! Proposals to decriminalise numerous company law violations are already underway and, with the oppressive angel tax regime being nebulised for startups raising funds—and tax officers being told to ease the whip during investigations—the stand of the government (although reactive in nature) deserves complete credit and gratitude.

I anticipate creativity in structuring of investment deals, to follow this change, in the universe of unlisted companies. For example, a Nike kind of corporate structure can be adopted suitably, wherein Class A shareholders have the power to elect 75% of the board. Alternatively, there could also be some interesting issues arising, where equity could be diluted below 50%, with the investors holding equal or greater strength at the Board level, but with the startup founders holding more than substantial voting rights at a shareholder level. A simple case of approving an amendment to a company's articles of association, therefore, could be met with a challenge, where, say, Class A shareholders of a company with DVRs could block a special resolution, through their voting rights being disproportionately higher, despite equity dilutions following multiple rounds of capital raising. The proposed SEBI framework does advert some of these challenges due to mechanisms such as the coat-tail provisions, which allow for flattening of the voting rights in some situations.

A protectionist regime in favour of domestic founders is only fair at a time when countries and continents face de-globalisation and trade wars at a macro level. It is also a great way to ensure effective control of a company is retained with entrepreneurs regardless of enormous rounds of funding, by allowing for a separation between stock ownership, economic rights attached to such stock, and voting control.

There are various other aspects which, I believe, will come into play going forward. For instance, how would superior voting rights shares be valued? Would they be taxed higher at the time of their sell down? Could VC investors look to set off superior voting arrangements against a higher contractual liquidation preference during deal negotiations, assuming disproportionately higher liquidation preference could be read within the ambit of how DVR shares are defined under the law?

Needless to say, a new era of capital raising has begun, thereby allowing for more Silicon Valley inspired investment structuring and negotiations. Sell-side deal lawyers and founders rejoice!

LETTERS TO THE EDITOR

Amazon wildfires

The unprecedented fires in vast stretches of the Amazon rainforests, covering an area of some 5.5 million square kilometres—the world's largest—constitute an international environmental crisis of enormous magnitude. The damage these fires cause to the eco-system is immeasurable. The Amazon forests produce 20% of the earth's oxygen and are rightly called the 'earth's lungs'. Evidently, the fires deplete the forests' carbon-storing capacity, accelerating the pace of global warming. The Amazon forests produce 20% of the world's fresh water too, are also rich in wildlife, and home to one-tenth of all species of flora and fauna. The importance of protecting the Amazon forests cannot be overemphasised. Vast majority of the record number of wildfires do not occur naturally, but are caused by humans. Conservationists and climate activists blame the new right-wing Brazilian government for the anthropogenic fires. It is evident that Bolsonaro government is lukewarm about dousing the fires. Fires are raging at a record speed and an area of roughly the size of a football pitch is now being lost every single minute. If no timely action is taken to put out the raging fires and prevent them from spreading, the Amazon forests will be reduced to a treeless plain, a savannah disrupting the delicate balance of nature. If Brazil is unable to protect the Amazon forests, an important natural treasure as well as a crucial life-supporting system on the planet from the fires, the global community is quite within its rights to intervene to protect them.

— G David Milton, Maruthancode

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PORTRAIT: SHYAM

COOMI KAPOOR

One for all...

From abiding friendships with many fierce rivals in politics to pals and protégés in court and Cabinet, Jaitley won hearts across all divides

IN MY LAST interaction with Arun Jaitley less than a month ago, he made a stray comment which could well serve as his epitaph. He said he made it a point to help whenever he was in a position to do so and he had been amply rewarded by the goodwill he enjoyed—he was speaking in the context of an opposition leader who found himself friendless in his recent legal difficulties.

Jaitley, 66, was a man who touched the lives of most with whom he interacted. At the All India Institute of Medical Sciences, as news of his death spread, people from all walks of life—from ministers and tycoons to party workers, lawyers to family friends—wept openly as they crowded the corridors of the hospital to pay their last respects, with security at a minimum. The moist eyes and ashen faces in the spheres in which he once held sway—the courts, Parliament, the cricket fraternity, the media, the Lodhi Gardens, the world of commerce, the corridors of power, BJP offices—reflect the universal affection in which he was held. A lawyer who has fought many legal battles against Jaitley's government told me at the hospital today, "He was the last good man in politics."

He was one of the most generous men I knew, ever ready to extend a helping hand. Many of the people he mentored are today in key positions in government, several ministers in Modi's cabinet are his protégés. His former juniors in the law practice have risen high in the profession. He was proud that the children of his office staff had performed extremely well in their respective professions, thanks to his generosity and encouragement.

Jaitley was among the first to appreciate the talent of Narendra Modi when he was a faceless party general secretary in Delhi in the 1990s. In 2010, when Amit Shah was briefly externed from Gujarat, one often found Shah sitting in a corner of Jaitley's office in Parliament. Till almost the very end, Jaitley remained in regular touch with the prime minister and the home minister, even though he had refused to accept any ministerial post in the new government because of his failing health.

He may have been a member of a party that's considered by its detractors as closed-minded, but he himself remained a liberal humanist, always ready to listen to views which differed from his own. Once when I commented that he was looking very grim in a newspaper photograph in which he had an elaborate saffron headgear, he admitted candidly that he felt uncomfortable with such trappings. When others in his party were bending over backwards to prove their party loyalty during the controversial 2017 vote for a Rajya Sabha seat from Gujarat—Ahmed Patel was the Congress candidate and the BJP resorted to some arm twisting—he was asked by a journalist in Parliament on which side was he on. He replied simply, "I am for democracy." His enlightened, flexible touch, which often softened his party's rigid and dogmatic approach, will be much missed in the government.

He had many close friends across the political divide. Pranab Mukherjee, as the UPA's finance minister, confessed at an Idea Exchange programme of *The Indian Express* that the man he most admired from the Opposition ranks was Jaitley, then Leader of the Opposition in Rajya Sabha. As a student leader during JP's agitation, he became close to fellow students from Bihar, Lalu Prasad Yadav and Nitish Kumar, who were his contemporaries in the movement. Congress leaders such as Jyotiraditya Scindia and Rajiv Shukla were family friends.

Amarinder Singh may have defeated him in the Amritsar Lok Sabha constituency in 2014, but the two remained in touch. He had a long association with the Badals of the Akali Dal. His numerous contacts benefited his party in stitching up alliances, reaching political agreements and fire-fighting. For instance, at a farewell dinner for Pranab Mukherjee as President in 2017, Jaitley tipped off Nitish Kumar that Lalu Prasad was planning to break his party. In the bargain, Jaitley sewed up an alliance between the JD(U) and BJP in Bihar.

He was always a favourite of the media. Parliament correspondents would wait eagerly for him to make an appearance in Central Hall in the afternoons, since he invariably had some juicy tidbit to relate or a humorous anecdote which had not escaped his eagle eye. He was a brilliant raconteur who was the centre of attraction in many a gathering, whether in Lodhi Gardens after a walk or at a dinner party. He had intimate knowledge of men and matters, partly because people tended to confide in him and partly because of his prodigious memory. The term "Khan Market set" was first coined by him, as were many other such witticisms. Such was the goodwill he enjoyed in the legal fraternity that when he campaigned for the Amritsar seat in 2014, scores of Delhi's top lawyers took time off from their high-paying billable hours to stomp the streets of the city for him.

During Modi's first government in 2014, Jaitley was the PM's trusted point person with the Opposition and the media. He was also a sounding board for many government appointments since Modi was new to the Capital's corridors of power. It was indicative of the faith Modi reposed in Jaitley, as perhaps also evidence of a lack of experience in the Cabinet, that in the initial months, Jaitley was put in charge of the heavy portfolios of finance, commerce and defence and also asked to look after the information & broadcasting ministry temporarily.

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My first introduction to Jaitley was back in 1974 during Indira Gandhi's regime when I was a cub reporter and covered the victory of the handsome, articulate student leader from the ABVP, who had defeated the NSUI candidate, Brij Mohan Bhama, in the Delhi University Students Union election. In those days, Congress organisations dominated every sphere, so the victory was a major breakthrough. And unlike many student-politicians, his academic record at the prestigious Shri Ram College of Commerce was equally impressive. As a student leader, Jaitley played an active role in the JP movement. When Emergency was declared on June 26, 1975, there was a warrant out for his arrest. He escaped police by jumping over the rear wall of his house. Nevertheless by midday, he organised a student rally in Delhi University against Indira Gandhi. He spent the next 19 months in jail, but never let imprisonment bring his spirits down. As he once observed to me, "You could create your own world inside the prison. If you were young and thinking of fighting the Emergency, you did not get demoralised." In jail, he continued with his legal studies, got a first class in his second-year law, and made friends with people from various Opposition parties. He also met my husband Virendra Kapoor, a fellow MISA detenu, and they remained lifelong friends.

After the election of the Janata government in 1977, Jaitley completed his law degree and established himself as a promising lawyer. *The Indian Express* founder Ramnath Goenka, struck by his acumen, appointed him as the newspaper's legal adviser. By 1980, the newspaper was fighting the Indira Gandhi government on several fronts. Jaitley was in and out of the Express building, a part of which the government even threatened to demolish. He carefully vetted the newspaper's major campaigns against the powers that be to ensure that nothing was libellous. He always retained a special affection for the newspaper, even when he did not always agree with its views.

It was V P Singh who, as prime minister, gave Jaitley his first big break in the profession by appointing him additional solicitor general in 1989 at the young age of 36. Jaitley played an active role in the Bofors investigations. When Atal Bihari Vajpayee was sworn in as prime minister in 1999, Jaitley did not always get the positions he might have aspired for—he was seen initially as L K Advani's man and Pramod Mahajan, who had the blessings of the RSS, viewed him as competition. But when given responsibility as a minister of state in portfolios such as law, information & broadcasting, and corporate affairs, he proved his mettle. When his party was out of office, Jaitley, apart from being the party general secretary and one of the chief spokespersons, also pursued his legal practice. He was regarded as one of the country's leading senior counsel. One of his juniors recalls with awe his elephantine memory and his ability to grasp the crux of a case in a few minutes of reading a brief.

In 2009, his party appointed him Leader of the Opposition in Rajya Sabha and he had to give up his legal practice, which meant a considerable financial sacrifice. Though he did have a weakness for collecting expensive pens, watches and shawls, his culinary tastes were simple with Amritsari fish and bhatura being his favoured menu. There was never a hint of corruption throughout his career. Arvind Kejriwal once alleged that there were malpractices when Jaitley headed the Delhi District Cricket Association for 13 years. Facing a defamation case, the Delhi CM sheepishly apologised.

When Modi was sworn in as prime minister in 2014, it was but natural that Jaitley would become a key figure in his government since he was one of the few party seniors who backed Modi all the way from the beginning. As finance minister, he was responsible for ushering in GST, considered the most important economic reform since liberalisation. With his legal background and friendly relationships with leaders across parties, he played a significant role in fine-tuning important legislation in both the UPA and NDA governments for a decade, including the Anti Defection and Triple Talaq Bills.

Jaitley was dogged by ill health soon after he took oath in 2014. He fought his health issues with fortitude and courage and never let the world know of the many medical setbacks he faced. Almost till the end, he never gave up hope and continued to fight the infections. His death leaves a vacuum in current politics which will be difficult to fill.

The slowdown is structural

Monetary and fiscal policy measures alone cannot do the trick. Sustained growth requires a reforms policy

SANTOSH MEHROTRA

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IS THE ECONOMIC slowdown a structural one or a cyclical one? This question has come up repeatedly, and there are not many who would like to believe that this slowdown is structural.

In order to understand India's recent slowdown, let us start with global growth trends pre- and post-global economic crisis (GEC). Following a decade of high growth before GEC and a swift rebound after it, many EMEs are seeing stubbornly slower growth since 2011. India is no exception, despite favorable terms of trade as oil prices fell. On the domestic front, the withdrawal of the fiscal stimulus put in place right after the Lehman collapse is relevant. But the problems since the stimulus withdrawal have demonstrated structural problems that need elaboration.

The real drivers of GDP are private consumption, private investment, exports, and government expenditure. Let us start with private consumption—most in the news recently. The surest indicator that this crisis is mainly structural is that real wages, both rural and urban, have been flat between 2012 and 2018 (the exact opposite of what was happening between FY05 and FY12)—primarily because non-agricultural job growth has been very low, compared to the earlier period (when 7.5 mn new non-agri jobs were being created annually and open unemployment was 2.2%). Non-agri job growth since 2012 has been 2.9 mn pa, and open unemployment rose to an unprecedented 6.1%, with youth rates double or triple that. Consequently, real wages for regular urban workers that had risen from ₹183 per day in FY05 to ₹226 in FY12 (a 24% increase), have actually fallen to ₹205 (or a 8.9% decline) between 2012 and 2018. Rural regular wages, which had risen by 13%, fell slightly. Urban casual wages in real terms had risen by 31% earlier, rose only 7.1% between 2012 and 2018. Rural casual wages had risen 44.5% before 2012 but barely rose 6% over 2012-18.

The current crisis is one of incomes, driven by poor non-agri jobs growth. While manufacturing jobs rose by 11% between FY05 and FY12, they fell by 5.7% between 2012 and 2018. Construction jobs that account for most of the jobs that rural migrants take up rose by 96.5% compared to 8% recently; services 18.6% *vs* 13.4%.

With wages and incomes down, people can maintain consumption only by cutting savings. So household savings fell from 23.6% (FY12) to 17% of GDP (2011-12 series), i.e. to levels prevailing in the early 1990s. Of this, financial savings as a share of GDP are 7.2%, or at levels prevailing between 1990-1997. Naturally, a second driver of GDP growth, gross fixed capital formation is down to levels before FY05, when the dream run began; at 28%, they are nearly 6 percentage below that in FY12. As income growth is lower, consumption is compressed or only maintained at the expense of savings. Despite private corporate savings having risen from 9.5% in FY12 to 11.6% of GDP, there is no "animal spirit" for investment growing faster.

Merchandise exports were lower over FY18 than in FY14 in $ terms; as a share of GDP they fell from 17.2% in FY14 to 11.6% in FY18. Can the fourth driver of aggregate demand, government expenditure, be expanded? There is a "silent fiscal crisis", and the non-discretionary revenue expenditure and off-budget expenditures leave little elbow room for capital expenditure, certainly by the Centre (budgeted FY20 capital expenditure to GDP is 1.3 as against 1.4% in FY19). The fiscal consolidation path cannot be abandoned; as it is, the public sector's draft on financial savings is nearly crowding out private investment (if there was appetite for it, to start with).

India's fiscal stance in the run up to GEC was pro-cyclical, with large increases in appropriate compensatory (e.g. MGNREGA, MSP) and also infrastructure expenditure, but tragically also one-off very large farmer loan waiver in 2008 (announced before the GEC broke). But growth pre-GEC had been robust, that fiscal space still existed to pump-prime the economy from late-2008 onwards. India's fiscal stimulus was large, its quality poor as it focused on revenue expenditure (the exact opposite of China); in 2013-14, the gross fiscal deficit was still 4.5% of GDP. In 2014, the government went into fiscal consolidation overdrive to bring the deficit down to 3.4% in FY19. Hence, there is still no fiscal space to use public investment to stimulate the economy now. This is one element in the current cyclical downturn. The second cyclical element is the outcome of monetary policy. In the aftermath of the GEC, a former RBI Deputy Governor has argued rightly that "Indian monetary policy could have tilted unduly towards the "easy" side and could have prolonged the expansionary monetary policy cycle for a longer period than what would have warranted". Together with the fiscal stimulus, it brought inflation in its wake, and RBI's inflation-targeting stance.

However, since the November 2014 "taper tantrum", the real repo rate rose to 4% from negative territory, and has remained at 2-3% in real terms since. This is an important reason why inflation targeting is recognised to have had a negative impact on growth rates. However, over-borrowing when the real interest was in negative territory post-2008 underlies the NPA-crisis. NPA-overhang is the foundational reason for low borrowing continuing; the NBFC crisis exacerbated it, especially for MSMEs.

Some short run actions are necessary, but will be palliative. On monetary policy, action is needed to reduce the repo rate. A real rate of borrowing of 2.5% cannot be conducive to borrowing when animal spirits are weak, and capacity utilisation running at 70-75% depending upon industry. There is some recent increase in credit offtake, and hence sharp rate reductions are necessary. Second, banks will have to transmit rate reductions, requiring an institutional mechanism (as the RBI Governor has indicated). Third, the rupee has to be allowed to depreciate slowly, since the rising real effective exchange rate has hurt exports. On fiscal policy, given the limited fiscal space, the only possibilities of raising revenues are of the non-tax type: monetise government and PSU land as rapidly as possible. Railways hold 10 mn hectares surplus that can be either sold or leased out, generating revenues over a long time. Second, the goal of divesting government equity in public enterprises and in PSBs will also generate resources for increasing public infrastructure investment—which should crowd in private investment. It could be partly used to recapitalise PSBs.

But monetary and fiscal policy measures alone cannot do the trick. A sustained growth path requires such measures fall within a medium term strategy, including an industrial policy and other structural reforms, especially financial sector reform. The strategy would not succeed unless agricultural growth is 4% plus pa. That requires a tilt away from the price- and subsidy-based current regime to a strategy-based one on public investment in agriculture.

India is nowhere close to a middle-income trap, that some economists have argued it is in. We have the potential to grow at 7-8% pa in real terms, and thus potentially become a $5 trn economy in five years.