Opinion

WEDNESDAY, OCTOBER 16, 2019

TROUBLED WATERS

Prime minister Narendra Modi

For 70 years, the water which belongs to India and the farmers of Haryana flowed to Pakistan. Modi will stop this water (from flowing into Pakistan) and bring to your houses

RationalExpectations

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Poor Economics vs Good Governance

Banerjee-Duflo's models don't always work, but the Nobel is an affirmation of the need for evidence-based policies

UNLIKE MANY NOBEL prizes where the practical applications of the winning theory is not immediately clear, it is easy to understand why Abhijit Banerjee, Esther Duflo, and Michael Kremer won the economics award this year. Tackling poverty is a global goal, and governments such as those in India spend upwards of ₹300,000 crore—that is 2% of GDP by the Centre alone, the states spend a similar amount—every year on some form of welfare activity. So, it is important to make sure the country gets the biggest bang for its buck.

Over time, the trio's research—through the Abdul Latif Jameel Poverty Action Lab (J-PAL) in the case of Banerjee-Duflo—has pointed to what solutions work and what don't; on how to tweak delivery systems to make them better. Over time, the trio set up two groups of people in what is called a Randomised Control Trial (RCT)—one that get the benefits, and one that don't—to see just how well the action/intervention works. In the case of schools in Vadodara and Mumbai, in association with the NGO Pratham, Banerjee-Duflo's RCT established that providing tuitions for individual students improved overall test scores for the entire school dramatically. The reason, it turns out, is that most government schools have classrooms with children of different abilities—some have Class 2-level Maths skills, some class 3, and some class 6—so the class teacher doesn't know quite where to pitch the lesson; the remedial intervention solves for this by bringing all the kids to the same level. The Nobel citation talks of how "more than five million Indian children have benefited from effective programmes of remedial tutoring in schools".

In the case of Punjab, *The Indian Express* reports the *Pani Bachao Paisa Kamao* scheme is based on a J-PAL recommendation where farmers are paid a fixed amount for buying electricity, which is used to pump out water; if farmers use less electricity—which means they use less water—they get to keep the money they save. One farmer, Karamjit Singh Rai, earned ₹12,904 through this scheme. If such solutions were to be used across the board, the Nobel committee must have felt, the impact could be quite dramatic.

While it is heartening to see governments listening to the advice of economists like Banerjee-Duflo-Kremer, it is not as if RCTs don't have their fair share of critics. While RCTs try and eliminate regional and other biases by selecting two groups within the same area, solutions that work in one geography do not necessarily work in others; nor is it clear why a particular solution works. In Udaipur, when it was found that not enough women were getting their children in for immunisation even though it was free, Banerjee-Duflo's team gave those who came in some free *daal*; this seemed to work, and immunisation levels in the area rose fairly quickly. So, the obvious question is, would giving cash have worked just as well, and didn't the mothers think that free immunisation in itself was worth it? Indeed, if it is not, why is Swachh Bharat working as well as it is?

> **Interventions to improve education or raise levels of immunisation good, but policymakers need to see if a GDP- or jobs-focus is better. And, is it better to substitute most govt schemes with cash payouts like NYAY?**

Some of this is also intuitive. Agriculture economist Ashok Gulati, without the benefit of RCTs, has been recommending that the government give farmers a fixed amount of money each year to spend on fertilisers; once farmers know they will get the subsidy regardless of how much fertiliser they buy, Gulati argues, they will consume less fertiliser, and use the rest of the money for something else. As a result, the damage to the soil will also reduce. That is also why, more than five years ago, Gulati recommended the government scrap most of its agriculture schemes, like MSP-based procurement, and opt, instead, for a flat annual payment to farmers.

Nor do RCT-type of experiments always give a clear answer on the preferable policy option. Banerjee, for instance, helped the Congress design its NYAY election promise, where the poor were to get ₹2,500 per month as dole—the party raised this to ₹6,000 when announcing the scheme. So, is NYAY a better option than individual government schemes in various fields like education or health, or are the poor not smart enough to use the money well? For whatever reason, Banerjee never explicitly recommended using NYAY in place of other welfare-spend, or at least not publicly.

Yet, SEWA's pilot studies in Madhya Pradesh in 2012-13 found that villages that got untied cash transfers tended to open more bank accounts, build toilets (this was before Swacch Bharat began), use more modern fuel for cooking/lighting, send more children to school, etc. And, Gulati's study with Shenggen Fan and Sukhadeo Thorat found that, while every million rupees spent on fertiliser subsidies reduced the number of poor by 24, the reduction was 335 if the same money was invested in building roads, and 323 if it was spent on agricultural R&D.

While the policy lesson from the Nobel prize is that all government actions must be based on evidence—and must be junked if there is no proof of their impact after a reasonable period of time—it is important that policymakers also keep in mind the limitations of micro-actions of the Banerjee-Duflo-Kremer kind. Certainly, they will help alleviate poverty or suffering in the short-run, and they will make health and education spending more efficient—this is a very big positive—but they have to be used in conjunction with other policies to enhance growth. That is why, for instance, Banerjee opposed demonetisation since it reduced economic growth, and the biggest sufferers from it were the poor; no amount of welfare intervention can make up for the loss of livelihood. Also, larger government spending on building roads or creating Aadhaar-like solutions create their own virtuous cycles that help the poor. Eventually, good governance creates good economics for the poor; given how little economic thought has gone into most pro-poor schemes in India, Banerjee-Duflo's defining work on fighting poverty is called *Poor Economics*.

BandAID

Giving away FCI grains as aid is a temporary solution; price support and PDS reforms are key in the long-term

WITH FCI'S GRAINS stock hitting unmanageable levels, the food ministry has asked the external affairs ministry to explore the possibility of giving away some of the stock to "deserving countries" as aid. India has done this before, but at a much smaller scale than what is probably envisaged now. Giving away the grains—for a country ranked very low on the Global Hunger Index, this may not be great optics—is still a better option than allowing it to rot. Rather, the government should be thinking of reforming its procurement/price support policy. Against stocking norms requiring just 307.7 lakh metric tonnes (mt) to be held in the central pool on October 1, the total was 669.15 lakh mt on September 1. Worse, thanks to bad policy, FCI's outstanding debt in FY19 stood at ₹2.2 lakh crore.

Procurement policy has meant that existing storage remains perpetually inadequate. One solution is to liquidate the huge surplus, but FCI's open market sales scheme failed to take off as prices of wheat and rice in the open market don't cover the economic costs of FCI procurement and storage. Worse, exports also can't be an option—even when the grain-quality issue is overlooked—because the price support policy means exports won't meet WTO norms. Unless the Centre considers reforming its MSPs and PDS policies, replacing them with, say, DBT for food and cost-support to farmers, respectively, FCI will keep facing this problem.

AILING GROWTH

WITH CREDIT MULTIPLIER STAYING WEAK, IT IS TIME TO WORRY IF CONTAGION FROM THE FINANCIAL SECTOR TO THE REAL SECTOR IS SPREADING

Economic growth in a critical phase

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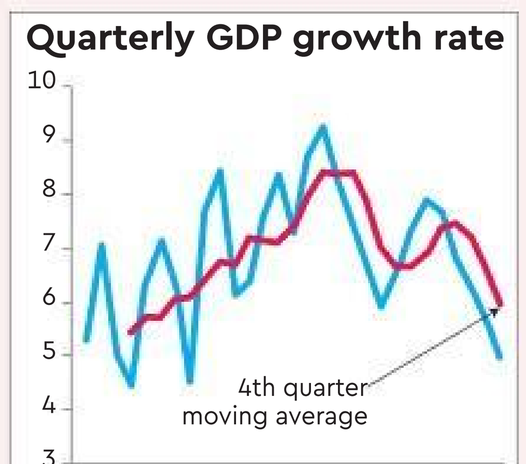
Views are personal

NEWS ON WEAK domestic economic activities continues. Judging by leading real and financial indicators, it seems certain that Q2FY20 growth would be worse than last quarter's 5%. Currently, most forecasts hope for a quick turnaround in H2FY20 from a supposedly cyclical slowdown, a popular first line of explanation that economists dish out. RBI's sharp cut in FY20 growth projection to 6.1% will not hold for long; another downgrade will most likely follow in December, after the release of second-quarter GDP estimates. Even as the forecast error relative to over-optimistic initial growth projection (above 7%) magnifies, the underlying narratives haven't changed much—the slowdown is still cyclical, but with a much larger output gap!

What if the slowdown is more structural? If so, potential growth should be declining, i.e., weakening trend. The accompanying graphic clearly supports such a view—the Q1FY19 peak, at 7.4%, was 100 bps lower from the preceding peak, Q1FY17 (8.4%). One can quibble about the statistical finesse of this simplistic assessment, but the trend slowdown is unmistakable. The real question is if it has fallen further after the recent growth shock. There was always a question mark on the claim of higher potential growth rate amidst weak private investment, and consistently lower capacity utilisation; its sudden collapse supports the contention that it was pushed by higher government spending, and credit by NBFCs.

For quite some time, RBI has been careful not to make its potential output estimates public, speaking in terms of the output gap. But, its projection of a sharp recovery to 7% in FY21 indicates RBI believes the economy's potential remains intact! This recalls a recent phase in which most analysts, including us, went horribly wrong on inflation forecasts! RBI, too, kept projecting higher inflation, anticipating a rebound in food inflation that was long dead. Consequently, monetary policy remained overtly tight for too long, lasting several quarters. In hindsight, one could argue that those policy errors possibly contributed significantly to the subsequent slowdown!

Quarterly GDP growth rate



Source: CSO

This makes one speculate if RBI, and others, are making similar errors in H2FY20, and FY21 growth forecasts. With inflation projections, the gap in actual and forecast errors kept increasing, but MPC was unwilling to amend, sticking to its structural model built around the ghost of food inflation bounce-back. Now, error between actual and forecast GDP growth keeps amplifying each quarter, but policy makers stick to 'predominantly cyclical' description of the slowdown. A widening output gap creates ample space for countercyclical responses; it prompts MPC to ease more, and government to seek fiscal stimulus opportunities, largely off-budget.

Ordinarily, any countercyclical response to structural slowing would invite higher inflation, and related uncertainties. But, many believe there is an extraordinary phase of weak inflation; this could absorb any potential fallout of countercyclical policy error. The risk is worth taking, they reason; bigger policy rate cut, and some on-budget fiscal expansion could quickly close the output gap. Such thinking would appeal to a government looking for a quick turnaround, but underlying risks could multiply manifold and blow-up in the medium term. Inflation may have been tamed, but inflationary expectations are still very high! One shouldn't forget the post-2008 experience, when UPA-II fired many countercyclical measures, raising demand through unflinching credit expansion and fiscal boost, which created a mirage of higher trend growth while real potential remained well below. What followed was an inflation spiral, growth crash, and external account pressures. Adherence to cyclical accounts could be laying the ground for repeating historical mistakes.

Some argue that even if this is a structural slowdown, the real rate remains too high; there is enough space for further easing. We, alongside this newspaper, consistently advocated such a view for several years. But, that time has now passed: Monetary policy has lost its mojo. Even with MPC further lowering the repo rate and RBI forcing banks to immediately transmit through external benchmarking, little is going to change on the ground. Just see the recent policy rate cycle: the MPC eased 160 bps from June 2018 to August 2019, when the credit channel remained completely blocked. The "Flow of Financial Resources to the Commercial Sector" graphic in *Monetary Policy Report*, October 2019 that has invited much attention shows how RBI's obsession with inflation targeting (IT), another structural reform in Modi 1.0, has gone haywire.

IT advocates constantly assured that once macroeconomic stability is durable, growth dividend would follow via lower cost of capital, and stable bond market. What happened? One can understand bank lending rates not falling much because of high NPAs and their slow redressal, but why did treasury yield not crash in line with falling inflation?

Focus has now shifted to the Centre's off-budget spending, and quasi-sovereign borrowings by public sector undertakings, viz. public sector borrowing requirement (PSBR). Eagerness to play by letter, not spirit of the Fiscal Responsibility and Budget Management (FRBM) Act is at the centre of the blame game. If governments, Centre and states (about whose off-budget borrowings, little is known), were to capture most financial savings, crowding-out is no more "psychological". It is real, and embedded in high bond yields. Rising debt, and falling tax revenues have virtually shifted the economy's lever to the bond market! More OMOs, liquidity management tweaks through additional tools (e.g. forex swap) are only temporary reprieves.

Opinion that the current fiscal logjam can be navigated by scaling up divestment is not a great strategy either. With financial savings dwindling, where is the scope for further raising PSBR? More asset sales will only squeeze private corporate savings directly for public capex; this is currently happening through PSBR, but indirectly, through bank borrowings and bonds. This may please fiscal hawks, but macroeconomic gains would be marginal. The government may have the satisfaction of building more roads and railways, flaunt more statistics, but the economy's potential will not raise much unless private investment is back in the game!

This should make it abundantly clear to votaries of the cyclical prognosis that fiscal space is more or less closed. Policymakers must accept that the FY16-FY18 growth acceleration increasing PSBRs and fuelling credit through NBFCs was never sustainable. That the NBFC credit cycle busted even before public banks' balance sheets were adequately repaired shouldn't have surprised anyone. With credit multiplier staying weak, they should worry if financial contagion is spreading to the real sector.

Forcing credit through "Loan *Melas*" is not the way forward. This will further erode credibility of PSBs. The focus must shift to structural reforms. To the government's credit, it implemented several key reforms, small and big. Unfortunately, textbook reforms like inflation targeting, IBC, RERA, and GST have not yielded expected growth dividend. More structural reforms are welcome, but we must know why current ones underperformed? Likewise, more roads and railways have been built, yet these haven't added to the potential; at least, not so far. It is a mystery why consumer and business sentiments nosedived after re-electing a popular government; one bad budget couldn't have pulled down confidence so much. It is time to introspect if we are misdiagnosing the problem over and over again!

In need of a new development index

If we want leaders to consider how badly their policies are damaging the environment, we need a new development index

AJAY CHHIBBER
Bloomberg

AT INTERNATIONAL MONETARY Fund and World Bank meetings in Washington this week, there will be much debate about slowing global growth, the impact of the US-China trade war, the role of central banks in preventing a global recession, the risk of disruption to oil markets, and much more. What you won't hear, beyond a few platitudes, is a detailed plan for combating climate change and slowing the depletion of the earth's resources.

This pattern of neglect won't change unless we do a much better job of linking the climate to economic progress. That in turn will require changing the way we measure development.

The world still looks at human progress in almost exclusively economic terms. Countries view growth in their stock markets and their GDP per capita with chest-thumping pride. Almost three decades ago, the United Nations Development Programme tried to produce a more nuanced measure of progress by including life expectancy and education along with income in its Human Development Index (HDI). While a welcome innovation, the original HDI is still relatively crude, failing to account for such things as sustainability and inequality.

How much those omissions can matter became clear recently, after the UN added an inequality-adjusted index (IHDI) to its *2018 Human Development Report*. Including inequality as a factor dramatically altered countries' rankings. The US, for instance, fell from 13th on the original index to 25th on the adjusted one. By contrast, Finland rose from 15th to fifth place.

Accounting for climate damage would likely have an even bigger impact. Countries that rank high on the human development index also use more carbon and deplete more natural resources than those below them. In other words, our metrics favour unsustainable, environmentally damaging growth. (Using more energy also produces a higher ranking, but only up to roughly 100 gigajoules per person; beyond that, countries are wasting energy in inefficient systems, not improving human development.)

The same applies to the relationship between the HDI rankings and a measure known as an "ecological footprint." Up to the middle of the list, where around 140 mostly low- and middle-income countries sit, the footprint is relatively small, less than 2 global hectares per capita (a measure of the world's global ecological capacity per person). That number rises sharply among countries with higher development levels, however, increasing to as much as 8-10 global hectares.

If we want leaders to consider how badly their policies are damaging the environment, we need a new development index, one that takes account of various environmental variables such as CO_2 emissions per capita, SO_2 emissions (a measure of air quality), groundwater extraction and share of renewable energy. Doing so would drop the rankings of countries from the US to Kuwait, Saudi Arabia and Australia by over 15 spots apiece. If the ecological footprints of countries were considered, the rankings of Canada, Estonia and, surprisingly, Finland in addition to those countries would drop by over 20 places.

Other attempts to produce a more sophisticated measure of development haven't gotten traction. While the UN agreed to pursue its Sustainable Development Goals in 2015, the system—which includes 17 goals and 169 indicators—is too complicated to measure succinctly. The Happy Planet Index hasn't gained wide acceptability because it mixes observed data on things like life expectancy and inequality with survey results measuring well-being. (Its rankings show Costa Rica and Vietnam in the top two positions, with New Zealand the only fully industrialised country among the top 20; the US ranks 105th.)

A Social Progress Index, inspired by the writings of Nobel-winning economists such as Amartya Sen, Joseph Stiglitz and Douglas North, produces rankings that don't differ all that much from the HDI. The World Bank has introduced the concept of adjusted net savings to measure changes to wealth (a stock) rather than GDP (a flow), while accounting for additions or depletion of natural capital. But, the measure doesn't adequately address the huge stock of accumulating CO_2, SO_2 or methane in the atmosphere, the country-sized swarms of plastic now floating in the oceans or the melting of glaciers—all things that show we may be at an environmental tipping point.

Over the last 30 years, the shift from looking just at GDP to judging countries on health and education outcomes has produced real progress, as the world has improved its human development index by over 20% since 1990 and, more meaningfully, in the least developed countries by over 50%. If we want real action on climate, we now need to include damage to the environment and depletion of natural resources as factors in measuring development. Otherwise all these fine-sounding speeches are just more hot air.

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LETTERS TO THE EDITOR

Economics Nobel

Awarding this year's Nobel Prize for Economics to Abhijit Banerjee, Esther Duflo and Michael Kremer for their 'experimental approach to alleviating global poverty' came as an uplifting piece of news. Their researches and experiments guide governments and NGOs on how large-scale poverty can best be combated. The very subject of their work—improving human development indices—lends their seminal contributions a humanitarian touch. Their work goes beyond 'analysis' of poverty (theoretical economics) to 'mitigation' of poverty (applied economics), if one may put it so, and raises the hope of a poverty-free life. The recipients of the award have specialised in 'development economics' as well as 'behavioural economics', of which 'randomised control trials' (RCT) are a key component, to find out the 'incentives' that did and didn't work. RCT is not the panacea for poverty eradication; it is a tool to carry out test studies and assess the possible outcomes in a given situation to aid framing of policies, and facilitate the process of poverty eradication. Banerjee was highly critical of demonetisation, following which the economy went into a tailspin. He also took objection to the revision and suppression of 'inconvenient' data. In his view, the Indian economy is on a shaky ground with all-time low investment, job creation, and consumption, and is unlikely to revive despite the piecemeal measures to pull the country out of the crisis.

— G David Milton, Maruthancode

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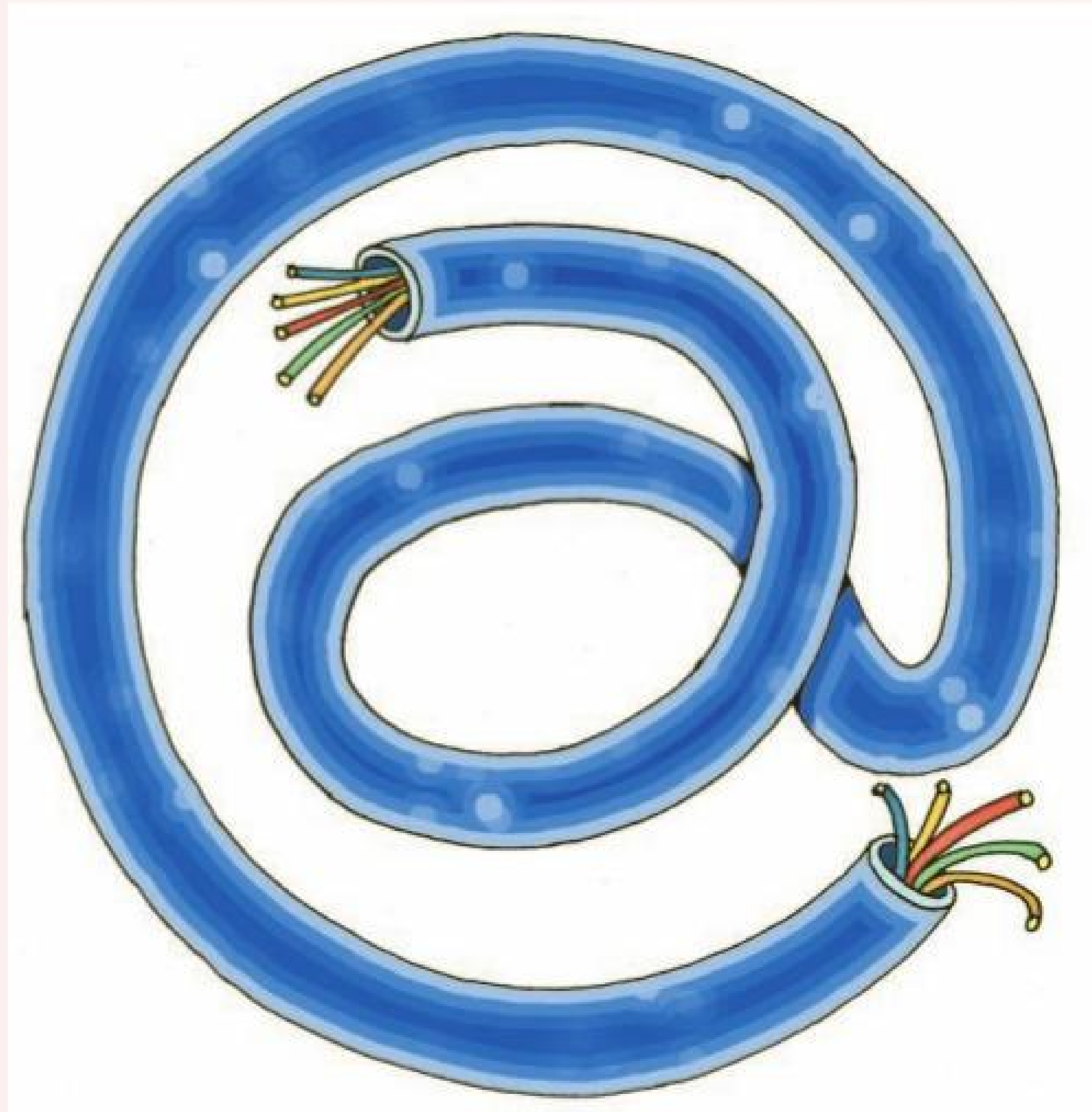

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FIBRE-TO-THE-HOME

Shared fibre infrastructure is key

The govt should ease the creation of independent, fibre infrastructure company (-ies) to be used by service providers. This will make the business a low-cost proposition and encourage telecom players to participate

ON SEPTEMBER 5, 2019, India launched fixed broadband fibre-to-the-home (FTTH) services by wireless operators. Let us examine the future of fixed broadband services in India over the next six years.

In the last four years, mobile operators upgraded India's wireless internet access services with an investment of over ₹6 lakh crore, attracting nearly 600 million mobile broadband consumers. As a result, the country's overall internet traffic volume has crossed 200 petabytes per day, second only to China.

This fast-paced adoption of the digital lifestyle boosted the digital entertainment and media market, with over 30 OTT players having mushroomed in this period. Today, at 10 gigabytes per subscriber per month, India boasts of the highest data usage on the small screen globally.

Yet investments in wireline business have hardly even approached full potential. India has only 18 million of the >1 billion global wired broadband subscribers. Of these, 10 million access internet on lower speed co-axial copper cables. As for FTTH penetration, India's presence is even weaker, with only 1.3 million FTTH households against over 350 million in China.

While telecom consultants, broadband experts, and many financial analysts estimate India's fixed broadband market to expand to 50 million by 2022, and 100 million by 2025, we see a clear gap between the visible consumer demand and fragile supply of fixed broadband FTTH services.

Indian digital consumers want access to whole gamut of video content anytime, anywhere, and seamlessly across devices at 50-100 Mbps or even higher speeds.

OTT players have forced traditional media and broadcasting companies to revisit some of their core business assumptions; cable and DTH Pay TV service providers are also trying to convert normal TV sets to smart TVs. This cord-cutting phenomenon, a rage in the western world, is expected to trend in high-income urban Indian households.

KPMG's India Digital Future Report 2018, Mass of Niches expects the native digital segment to shift from passive consumption to deeper engagement. Of the projection of 820 million digital users by 2025, they estimate 425 million to be wireless broadband customers, and over 100 million households to be highly engaged digital users. These 'Digital Enthusiasts', primarily millennials and Gen Z individuals, with >₹5 lakh pa incomes are more likely to pay for wired and wireless broadband services and OTT content.

The wired broadband revenue market size is projected to grow at a CAGR of 23%, expanding from ₹11,000 crore in FY18 to ₹50,000 crore in FY25. These projections appear plausible as the large screen device experience becomes even more exhilarating with UHD 4K content combined with enhanced multiplayer gaming experience. Households will transition from paying ₹500 per TV set to their Cable/DTH operator, to a home broadband service at ₹700-₹1,000 monthly ARPU for the entire household, with an additional ₹200-300 for OTT services. This will increase the average Indian consumer's monthly data consumption from 10-12 Gigabytes on a 4-6-inch wireless smartphone to 150-200 Gigabytes of usage at home. Globally, as per Cisco's 13th Annual Visual Networking Index (VNI) report, 69% of data traffic of 123 Exabyte per month is generated from fixed broadband services —India's trend in the long run can be no different.

Two or three integrated telecom operators are indicating early interest to tap the Indians' unmet demand for FTTH. In the past, Indian home broadband market remained underdeveloped due to absence of organised cable industry, which still remains fragmented and undercapitalised. With FTTH, globally fixed broadband services have evolved to become fast and reliable, with speeds ranging from 100 Mbps-1 Gbps, leading China, Indonesia, Malaysia, Korea, and Japan, among others, to adopt it. For example, in China, 81% home broadband users are on FTTH, and even developing nations, like Indonesia, Brazil, Thailand, Mexico, South Africa, Turkey, Vietnam, etc, are adding over 1 million fixed broadband FTTH subscribers per quarter consistently since last year.

What, then, is holding back Indian FTTH market growth? While demand for enhanced home broadband network and OTT services is not in doubt, the business case for next-generation Indian FTTH services remain unconvincing. As per an E&Y study, India's construction cost to reach a FTTH household is among the highest in the world at $1,580, i.e., ₹1,10,000, against $200 in China, $307 in Thailand, $334 in Indonesia, and $432 in Malaysia. The reasons for high FTTH rollout cost in India include exorbitant cost of RoW, high lead time for approval, uncooperative building societies, unorganised/expensive fibre construction services, high fibre maintenance cost, etc.

While private FTTH operators need support from the municipality, state government, the Centre, and the telecom regulator, fixed broadband operators can take advantage of the significant overlap between the coverage and footprint requirement of 4G today and 5G wireless broadband providers in future.

Studies across many markets show that wireless broadband access and fixed broadband access, both at home and the enterprise, are complementary services, not substitutes. Consumers will continue to use mobiles to access internet for short-burst data requirement, but will prefer home broadband services with OTT content for two-three hours per day of television viewing. However, India's wired broadband revenue opportunity will remain a pipedream unless service providers converge multiple fibre-based networks onto a unified footprint.

There are only one or two serious players trying to address the fibre supply challenge. However, the need for FTTH broadband services is being felt throughout the country. It is not possible for one or two players to allocate scarce financial capital to address this large demand while meeting capex requirements for India's future 5G technology rollout. The existing high-cost business model for fixed broadband services supply will not yield the desired 100 million FTTH households anytime soon.

Key to home broadband market success is availability of fibre infrastructure that can encourage multiple players to serve this large FTTH market. There are two possible models:

1. The FTTH provider itself does it, making end-to-end fibre available across 1,000+ towns in each residential and commercial complex. This model is expensive, with payback period of over eight years even at an annual ARPU of ₹12,000, and involves duplication of resources in large markets.

2. Replicating the mobility infrastructure model of pooled common resources instead of a fragmented one—private sector managing pooled fibre resources on long-term MSA contracts for dark fibre or leased fibre circuits.

Until the birth of telecom infrastructure providers in the form of independent tower companies like Indus and ATC, India's mobility voice presence was limited. This reduced the entry barrier for telecom players like Jio, Airtel, Idea, etc, enabling quick expansion of coverage through shared infrastructure without individual operators having to bear the capex burden of setting up their own towers. As a result, the telecom market expanded at an exponential pace between 2008 and 2015.

By converging multiple fibre-based networks onto a single- or two-network footprint, independently financed by private investors, this 'National Fibre Infrastructure' can ensure fibre availability across the country. Indian telecom operators have already built over 22 lakh km of fibre. As the country enters into the next phase of mobility growth, early interests in monetisation of non-core assets by telecom operators is being reported.

Passive Optical Network architecture already provides fibre sharing between many service providers through either Time Division Multiplexing or Wavelength Division Multiplexing. The current 22 lakh km of fibre, once transferred to a common pool managed by independent fibre infrastructure providers, will help support 1,500 petabytes of India's daily data needs, i.e., 7.5 times the current traffic.

Unless the DoT and Trai formulate regulatory policies to support growth of an independent fibre infrastructure company, this vision will not be realised. The challenge is to get multiple tenancies so that the infrastructure cost can be spread over a large number of operators. Fibre-MSA-cost to FTTH providers has to be a reasonable 60-70% of end consumer pricing. The DoT and Trai need to push central, state and municipal legislation to equate fibre deployment with infrastructure utility status. Policy could accord telecom optic fibre cable the status of public utility, offer a 10-year tax holiday to independent fibre companies, and encourage banks to leverage such companies to enable fibre-isation of at least 60% towers to reach 100 million households with FTTH. The National Building Code of India could be amended to make telecom installations and associated cabling mandatory for all commercial and residential buildings. A National Fibre Regulatory Authority overseeing setting up of common service ducts and utility corridors in all cities, apart from collaboration between states, the Centre and ULBs, will also need to be created.

Indian consumers are anxious to become part of the global FTTH revolution. With India's current fixed broadband business operating model, the gap between FTTH demand and supply will only widen unless a new collaborative, partnership-driven, low-cost business model and market structure become a reality. The government and regulator following the 'National Digital Communication Policy' vision will encourage FTTH services.

Pricing problem

AMIT BANSAL &SHRUTI GUPTA
Bansal is Partner and Gupta an Associate Director with Deloitte India.

The idea is to sift efficiency-enhancing pricing strategies from predatory pricing strategies

AS INDIA STEPS into the festive season and consumers plan big purchases, consumer goods companies are in a quandary over pricing. Consumers have exhibited strong preference towards online marketplaces for reasons attributable to discounted pricing, wider-choice set, and convenience among others. Discounts nowadays are ubiquitous and no longer characteristic of just promotional or introductory pricing.

Industry bodies have exhibited dissonance alleging that discounted pricing is 'destroying' and not merely 'disrupting' the market(s). The last few years have seen an erosion of margins in the consumer goods industry that traditionally priced its products relative to manufacturing costs. It is becoming increasingly difficult for traditional players to match the discounted offerings offered by their online counterparts. The source, the sustainability, and the distortionary impact of the discounting practices is questionable. Consequently, traditional market players have implored the Competition Commission of India (CCI) to rationalise discounts.

CCI has found it challenging to respond to these allegations because in most cases the accused are not dominant market players, and the Indian competition law in its current form is only applicable to dominant players (as also for anti-trust laws in more mature jurisdictions) that indulge in anti-competitive behaviour. Therefore, practices such as below cost pricing when practiced by non-dominant players, fall outside the radar of the current competition law.

Existing literature shows that predation may not be a rational strategy for dominant firms. A firm, when identified as dominant, is supposed to have pricing power and as such may never really be required to resort to predatory pricing.

Industry developments over the past few years demonstrates prevalence of deep discounting across sectors. In more mature sectors such as telecom, we are seeing the change in competitive landscape in the form of exit of few players, strain on financials of incumbent players and increase in consolidation. This phenomenon will make the market more prone to abuse by players that remain.

The timing of regulatory intervention is critical as it should not stifle market growth while at the same time not propagate creation of dominant players

Likewise, in the new age e-commerce space, we are observing that while the new businesses are struggling to make profits due to continued deep discounting, the traditional players are losing in the run-up to match competition and unable to keep pace to survive. This acquired market power will enable charging of high prices and in turn recoupment of lost profits in the future.

We have seen several instances of the CCI dismissing predatory pricing allegations at the prima facie stage due to lack of dominance by the alleged infringer. There is a need for ex-ante regulatory intervention in such cases.

Altering the competition law framework to encompass non-dominant firms may not be the ideal solution as it will unduly strain the time and resources available with the competition regulator. Allegations of new entrants or non-dominant firms indulging in predatory pricing may alternatively be evaluated in a manner similar to merger control.

The assessment criteria can be designed based on factors such as the financial position of the company (turnover thresholds), its antecedents, and its business model among other things. Like in the case of merger control, ex-ante effects based analysis can be performed. This will allow for the assessment of likelihood of exclusion of competitors and of possible recoupment of losses by the alleged predator. It will allow the alleged predator to put forth an efficiency defense.

We recognise that discounting prices often have competition and welfare enhancing effects. Price competition can force market players to innovate and bring about operational efficiencies, and therefore may not always reduce competition. Due caution will need to be exercised as excessive regulation may curb investment (and innovation), and hinder newer markets from coming into existence. The timing of regulatory intervention is critical as it should not stifle market growth while at the same time not propagate creation of dominant player. The idea is to sift efficiency-enhancing pricing strategies from predatory pricing strategies that have the intent of elimination of competitors per se and resultantly overcome the obstacle of 'under-enforcement' posed by the current competition law architecture.

NOBEL PRIZE

The right experiments

India should take pride in the evidence-based policy approach

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THE NOBEL PRIZE for economics this year goes for work on poverty which is probably the most serious challenge for the world. Therefore, there is a move away from behavioural economics, which has been popular with the jury and extensions of markets which has dominated the core work of other winners. In fact, there was some talk outside that the award would go to someone like Prof AK Sen. In an age when people are less enchanted with free markets and capitalism and economists like Thomas Piketty have occupied centre stage it is quite appropriate that Abhijit Banerjee, Esther Duflo and Michael Kremer have been accorded this award.

On the face of it, their work is quite simple. There are four parts to their story. First, there is need to identify the causes of poverty, second have the necessary interventions in place which can address the issue and third, carry out field experiments which work so that those which don't can be abandoned. The last is the cost-benefit analysis to evaluate efficacy. Accordingly, those which work can be persevered.

Poverty is a major issue for a large part of the human geography with over 700 mn people being afflicted in countries in Asia, Africa and Latin America. Over time several measures have been used to counter this problem with different modicums of success. The recipients work is based on carrying out experiments with solutions once the problem has been identified so that the policies become effective.

India can take pride in such an approach because over the years successive governments have been fighting poverty through different measures. In fact, while the awardees talk of identifying the problem first, in India we have the entire menu on the table: health, family planning, education, credit, agriculture, social security and so on. These have been on the agenda from the time of independence and in all our Planning documents.

Banerjee, Duflo and Kramer talk of interventions being identified and here too India has been fairly successful in formulating in different kinds of policies. Therefore, there are specific programmes for enhancing agriculture and various schemes are brought in to address health, education etc. New innovations have come through the NREGA programme or the PM-health scheme (Ayushman Bharat). One can even go back to the employment guarantee programme, minimum needs programme, Green revolution, etc. which were used in the seventies and eighties as the problems were well understood and were common to all states.

The third part of their thesis is that we need to carry out experiments to see how they work and integrate to make them effective. This is significant in India because we have the tendency to set monetary or financial targets which are achieved without being too effective. Hence, it is not uncommon to come across schools being constructed without having teachers and books and furniture. Teacher absenteeism is common. Policies, thus, fail to deliver. On the other hand several states like TN, AP, MP etc. have implemented the mid-day meal scheme which work well ensuring children attend schools.

India can be a good example, to show how poverty has been tackled. It tells policy makers what should be done and the safeguards that have to be built. While there is still reason for us to be dissatisfied on the state of poverty—300 mn are still deprived—credit has to be given for lowering the proportion given the level of leakages in the system which lead to wastages. In fact, the measures taken by the present government since 2014-15 to improve the distribution of fiscal benefits through better delivery mechanisms is commendable and can be a useful template to be followed across the country for all programmes.

Clearly, the road ahead is long for us and the Niti Aayog can take the thesis of these awardees as a template for evaluating all the programmes of the government and create a report card on the achievements and misses so as to improve the effectiveness of policy. Such an evaluation will help to sieve out those programmes that have not worked because efficiency parameters have not been met. The same funds can be routed to others which have worked or alternatively new programmes can be constructed. It is important to make every rupee of expenditure work with a definite cost-benefit analysis being in place.

The awardees have not added the willpower to get things done which is what is missing in most of the countries which have high poverty. In fact, in most of the countries in Africa and Latin America where the rulers are dictatorial, there is less incentive to bring about change which makes this goal a distant dream. In democracies like India a major challenge has been corruption which is what should also be addressed by countries to make their policies effective. Curiously most of the poorer nations have low scores in the World Bank Governance Index of the Corruption Index of Transparency International. Hence, there is a fifth dimension which is a practical issue that has to be appended to make such policies work in poorer countries.