Opinion

THURSDAY, NOVEMBER 28, 2019

WAR ON TERROR

Union defence minister Rajnath Singh

Terror incidents have been taking place in Jammu and Kashmir for the last 30-35 years. But I must compliment the forces. Terror incidents have now come down to almost nil (*lag bhag na ke barabar*)

US, China must act, or the world will fry

Latest UN report shows emissions growing, warming to hit 3.2°C by 2100 with current action

THE UN HAS been repeating its climate crisis warnings *ad nauseam*, but top global economies hardly seem to care. Its latest *Emissions Gap Report* states that greenhouse gas (GHG) emissions have risen 1.5% per year in the last decade, stabilising only briefly between 2014 and 2016. Total GHG emissions, including from land-use change, stood at the historical high of 55.3 giga tonne of carbon dioxide equivalent (GtCO2e) in 2018. This means more drastic cuts will need to be taken with each year of delay—at the current rate, emissions will need to fall by 25% and 55% from the 2018 level if the world is to stick to the least-cost path to limit global warming to >2°C and >1.5°C, respectively. Indeed, global GHG emissions must fall by 7.6% each year between 2020 and 2030 if the world is to keep to the 1.5°C pathway. The report also makes clear how abjectly inadequate the current action is; with current unconditional nationally determined contributions (NDCs), there is a 66% chance that warming will reach 3.2°C, if not more, by 2100.

The UN couldn't have stated it more squarely: "The summary findings are bleak... Countries collectively failed to stop the growth in global GHG emissions, meaning that deeper and faster cuts are now required." And, the highest degree of responsibility to act is that of the top global economies. But, the participation of G20 members at the Climate Action Summit held in September in New York is a sign of the climate betrayal playing out—the US, the host, didn't even speak at the summit. The latest UN report clearly names the US and China as the top emitters. While G20 economies being on track to meet their limited Cancun track should seem like good news—they account for 78% of the global GHG emissions—the US is one of the seven G20 countries that are currently projected to miss their Cancun Pledges or not achieve them with great certainty. Six, including China and India—India will overshoot its reduction target by more than 15%—are projected to meet their NDC reduction targets with current policies. But, the UN interprets this as a lack of ambition in targeting. Amongst the seven G20 members requiring additional policies and/or stricter enforcement of existing policies, the US has the largest gap to close, for both unconditional and conditional NDCs.

China emits 26% of the global GHG—the largest absolute emitter—and despite contributing significantly to the slowdown in emissions between 2014 and 2016, has seen emissions rise 1.6% in 2018. The US, the largest per capita emitter, saw a gradual decline in emissions of 0.1% per year in the last decade; but, in 2018, its emissions grew by 2.5%. While the US is quick to blame other nations, particularly, India and China—India contributes 7% of total GHG emissions, with a growth of 3.7% per year over the last decade—the fact is that the US and other developed nations, thanks to emissions over their respective histories of industrialisation, have shrunk the room for countries like India and China to grow without having to worry too much about the impact on climate. While the US's NDC target under the Paris Agreement was to reduce emissions by 26-28% from 2005 levels by 2025, its climate-denier president, Donald Trump, is leading it in "the opposite direction", having walked out of the Paris deal. The Clean Power Plan (CPP) of the Obama administration would have reduced power sector emissions by 32%; Trump's Affordable Clean Energy plan that replaced the CPP will more or less maintain the sans-CPP levels of emissions. The Trump administration's decisions on vehicle emissions and fuel economy standards will increase emissions from the transportation sector by 28-83 million tCO2e. It is true that 25 states in the US have joined the US Climate Alliance, a coalition committed to reducing emissions in line with the Paris Agreement, but unless there is commitment to act by the entire country—along with China, Canada, Russia and other economies that are failing to take ambitious action—the future seems quite bleak.

Staring down union blackmail

Telangana CM does well to hold his own on the TSRTC strike

GOVERNMENTS HAVE TYPICALLY yielded when held to ransom by trade unions. It hasn't been too different for the present dispensation at the Centre—be it in the matter of EPFO, where unions stonewalled the plan to allow provident fund subscribers to switch to NPS, or the coal sector employees' delaying entry of private sector in commercial mining. Given how trade unions have slowed the reforms process—as governments put political and electoral considerations before sound policy—it is refreshing that the Telangana government, led by K Chandrashekar Rao, didn't blink as employees of the Telangana State Road Transport Corporation (TSRTC) went on a strike demanding, among other things, that the loss-making TSRTC be taken over by the state transport department and they be given pay hikes. The state government had made it clear early on that it wouldn't allow such blackmail—indeed, Rao had given the employees an ultimatum, to join work before November 5 or face dismissal—and took swift action to deflate the unions' threat. So, even though this meant only a small fraction of the 10,000 TSRTC buses was plying the streets during the strike, and this was during the festival season, the Telangana government dismissed the striking employees when the deadline to join passed; instead, it ordered quick hiring of replacement staff, and even hiring of private operators to run TSRTC's fleet operations.

To be sure, the strike has exacted a large cost from the public, which has found transport options greatly shrunken, and some TSRTC employees even committed suicide in protest. But, at a time when the protest by Honda employees has caused a production loss of 70,000 units, such an unbending stand was perhaps necessary. This is not to paint the Telangana government as blameless; indeed, the TSRTC's losses are of its own making. Apart from forcing TSRTC to subsidise transport—subsidies totalled ₹526 crore in 2015-16—it even made transport free for certain categories of commuters. As losses built, the corporation was stranded for funds to upgrade infrastructure, with the state government looking the other way. A report on finances of state road transport corporations from 2015-16 shows that TSRTC, despite being one of the better performing road transport corporations, had employee costs that were 50% of its total revenue. With a staff per bus ratio lower than most states, this would suggest that TSRTC employees are perhaps also paid better than peers in other states. Rao, there is no denying, did right by not allowing the TSRTC employees to prod him into taking economically irresponsible decisions and throw good money after bad, but it would have been even better if his government had taken timely decisions on, say, fare hikes and infrastructure upgrades.

TRANSgression

The new law that was supposed to guarantee the rights of transgender persons actually undermines these

WHILE THE SUPREME Court's (SC's) judgment in *National Legal Services Authority (NALSA) vs Union of India* is considered a landmark for its progressive stance towards transgender persons, the Centre seems to have undone its gains by clearing the Transgender Persons (Protection of Rights) Bill 2019 in its current form. Instead of guaranteeing the right to self-determination of gender—this was guaranteed by SC in the *NALSA* case—the Bill vests the power to assign a person transgender status with the government. As per the provisions of the Bill, while a person can still self-identify to apply for a certificate, the actual granting of the certificate shall require an assessment by the district magistrate. In case the person undergoes a surgery, the DM will again examine the correctness of the medical certificate issued by the medical superintendent or chief medical officer. The humiliation of being denied legal status as a transgender person—likely for those who haven't 'transitioned' surgically—will have grave effects on the mental health of persons who already face social and economic ostracism, and sexual exploitation.

Not only this, the Bill's recognition of sexual abuse of transgender persons is also coloured. The legislation prescribes penalties for sexual abuse, and does not provide similar penalties for rape as those prescribed in cases where the survivor is a woman. The punishment, from six months to to two years, is also milder than that prescribed for sexual abuse of a woman under Section 354 of the IPC. Unless the government changes its approach, the new rules shall only impinge on the rights of transgender persons, not guarantee them.

INVESTOR ANXIETY

DIFFICULT TO GAUGE IF IT WILL SURVIVE THE RECENT DEMAND SHOCK, THE SEVERITY OF THE DEMAND FALL HAS DEPRESSED SENTIMENTS

Private investment in the doldrums

RENU KOHLI

New Delhi based macroeconomist

Views are personal

INDIA'S PREOCCUPATION WITH reviving investment goes back to over five years now. Since 2014, much fiscal-monetary ammunition, structural and other efforts have been expended to breathe some life into it. Yet, the share of gross fixed assets creation that sank 1.5 percentage points in FY13 to 32.6% of GDP (new series) is yet to get restored to even that lowered level. Last year, it reached 32.3%, inching 1.6 points in four years, from a 30.7% trough in FY16; this, too, mostly reflects public capex stimulus. When will private investment spring back? Why has all the hard work failed to achieve the intended objective?

In 2013, when aggregate investment sank −3.7%, it represented swelling uncertainty, besides deteriorated, unstable macroeconomic settings. *Inter alia*, sudden regulatory changes, retrospective tax legislation, a dysfunctional government delaying or jamming projects, other governance issues, and supply bottlenecks were major sources. Business confidence steadily fell after FY11. News coverage turned extensively negative, reporting these developments. Disentangling India's investment slowdown, the IMF employed a *Policy Uncertainty* Index based on news coverage, inflation, and budget deficit, finding that heightened uncertainty about the future course of broader economic policies and deteriorating business confidence played a significant role. Uncertainty, thus, mattered for investment.

Post-2014, inflation lowered, budget deficits restrained—at least officially (the CAG's revelation of significant build-up of hidden, off-budget liabilities came only last year)—and macro conditions stabilised. Stalled projects were cleared; hidden NPAs recognised with lagged resolution and recapitalisation; structural reforms like inflation targeting, GST, IBC, and RERA happened; business conduct was eased, along with other initiatives. These advancements were universally welcomed and endorsed. News coverage has been positive. Put differently, an update to the *Policy Uncertainty* Index would show it much lowered.

Then, why has investment not reacted to the improvement, the reduced uncertainty? Why does it remain unmoved in committing fresh capital? Why have structural reforms not worked?

One reason is the damaged balance sheets of banks and corporates, dating back to pre-2014 days; these are yet to mend, regain vigour. Meanwhile, the pace of resolution has infected other balance sheets, i.e., initial delay in addressing bad loans was compounded by asymmetric recognition and recapitalisation, wherein inadequate capital support slowed recovery of banks, who, in turn, restrained lending. Substitution through scaled-up lending by healthier non-banks to replace the bank credit deficit proved costly: Balance sheets here stretched too far, too quickly in taking on the banks' role. Non-banks raised outsized short-term funds to finance long duration loans, ending with asset-liability mismatches. Contagion has enhanced risk-aversion, credit deficit, and costs in other parts of the financial system, and for more participants.

Debt stress has also engulfed newer borrowers, viz. agriculture, small-medium businesses, and households that are burdened by falling incomes, and increased liabilities contracted at high real interest rates. Demonetisation, and a poorly designed and implemented GST, aggravated this situation. Borrowings-financed public capex spilled outside the budget, crowding out investment, and invalidating both fiscal and monetary stimulation; joined with low inflation, debt burden increased.

When responding agents are not in good shape, they are unlikely to react to supportive policy cues, and fresh openings from relative price changes induced by structural reforms. Reports of ICICI's closure of its project finance division earlier this month betrays the persisting risk-aversion to enduring exposure, and a possible demand deficit for long-term investments.

Other than balance sheet weaknesses, there are intangible or soft reasons for investor anxiety. Despite positive news coverage and macroeconomic betterment, there are layers of uncertainty, originating from perceptions of private businesses, about structural changes, disappointments over unmet expectations, lack of clarity and unease about the direction of economic policies.

In the financial sector, capital support for public banks has been universally assessed to be deficient to cover provisioning and growth. Hidden bad loans and unethical lending uncovered at private Indian banks exposed governance problems akin to public sector banks, perpetuating mistrust. Banking reforms, too, have either fallen short or are reverse of expectations, e.g., consolidation instead of privatisation; no indications on the future role/direction of public banking; procyclical regulatory changes antithetical to recovery and repair, sometimes amended or even withdrawn, contribute a layer of uncertainty in the financial sector. The NBFC crisis, its persistence, and continuing defaults add another coat of uncertainty. These have hardly imparted confidence to the private sector about how to proceed.

> The NBFC crisis, its persistence, and continuing defaults... have hardly imparted confidence to the private sector about how to proceed

The IBC is considered a huge positive step. But, it seems to raise uncertainty due to unanticipated and long-drawn legal tangles, constant amendments to refine the law, delayed timelines, and doubted outcomes. Unresolved problems in the power sector, fresh troubles and insolvencies in aviation and telecom, and fragilities in real estate, housing and infrastructure are another stratum of hidden, unspoken uncertainty. Tax terrorism is another layer. Uncertainty about the future course of policies towards public and private sectors also seems to have gained ground with more centralisation, the favouring and prioritisation of public over private sector. Key structural reforms missed out on—land, labour market, etc—dejected private ardour, too. Changes in rules, norms, regulation without adequate feedback or studying ripple effects added another film of uncertainty, as in the automobile segment.

Last, but crucial, is uncertainty about demand conditions. This is not merely statistical, the large gap in robust growth portrayed by new GDP data and high-frequency volume indicators, or the contested unemployment-consumption estimates. Conflicting signs from multiple sources have created confusion amongst private agents about actual demand. For any firm planning production or capacity addition, future demand, especially consumption, is a crucial input for volume, revenue and cost projections.

The inability to anticipate policies with precision or clarity sows doubts in business's mind, which is then likely to question a bet on committing money. The private sector perceives uncertainty as it sees collective policies and preferences in a longer timeframe.

Possibly, the plunge in business confidence in RBI's April-June survey may reflect these intangibles, besides the June budget shock that alone could not have triggered a drop comparable to the global financial crisis (2009) and the dotcom (2001) shocks.

The policy environment has turned since then. Unpleasant tax proposals were reversed, and replaced by supportive fiscal actions, notably business tax cuts. Further reforms, e.g., relaxing labour regulations, have happened; more are likely to come. Fresh expectations of investment revival are in the air. The uncertainty about demand conditions has evaporated—most information sources, including GDP, lead indicators, and corporate performance are converging to show universally steep declines in economic activity. Should we, then, expect investment to finally get restored?

Ironically, the disappearance of demand uncertainty or the sureness about demand, its all-round confirmation and the severity of its fall, has widely depressed sentiments and confidence in matching proportion. For now, the demand outlook is assessed to be grim. Importantly, there are doubts about what lies ahead: No one is sure if growth will further decelerate, recover to 7%, or languish at low levels. This scenario suggests that fresh changes, reforms must wait to yield results as agents await clarity. Very steep demand declines often require a substantial uplift to restore beliefs about future economic prospects, to which is linked the mood to invest. India would be fortunate if this comes about.

CHINA'S $-BOND SALE

The limits of the trade war

The US and China might differ on issues of trade and human rights, but the latter's sale of $6 billion of dollar bonds shows they are nowhere near being "in the foothills of a cold war"

BRIAN CHAPPATTA

Bloomberg

THOSE WHO FEAR an impending cold war between the US and China need only look to the bond market to see evidence of a potential thaw.

In the midst of a holiday-shortened week for American markets, China easily sold a record $6 billion of dollar-denominated bonds, accumulating $20 billion of investor orders that allowed it to tighten yield spreads for a lower borrowing cost, *Bloomberg News* reported. While hardly unexpected—this is the third straight time the country has borrowed in the US currency around this time of year—it nevertheless sends a clear signal to global investors that the ongoing trade dispute with the US isn't going to stop China from integrating itself and local issuers into worldwide financial markets. And, it likely suggests a limit to how far any sort of lasting tensions between the two largest economies can go.

China's Ministry of Finance has said one goal of its dollar-debt sales is to help build a benchmark yield curve for Chinese issuers. That would serve two functions: It would allow its multinational firms to raise funds in the US currency more easily, while simultaneously giving Chinese banks a local option to allocate dollar deposits. Thanks to this week's deal, which had portions due from three years to 20 years, China will have now have dollar debt that matures from 2022 all the way to a small portion in 2096.

It is important to remember that China doesn't need to do this. It has all the access to the greenback it would likely ever need in the form of its $1.1 trillion of US Treasury holdings. Selling a sliver of its treasuries would effectively serve the same purpose as a dollar-bond sale, only it would somewhat weaken the link between the two countries. Creating the foundation for a more robust dollar-debt market in China, on the other hand, does the opposite. Already, that market exceeds $740 billion, with sales in 2019 on pace to reach an all-time high.

Even at this massive size, Chinese dollar bonds (and those from other countries, too) are still ultimately subject to the whims of US officials. Earlier this year, the Trump administration was reportedly discussing ways to limit US investors' portfolio flows into China, such as by delisting Chinese companies from US stock exchanges and limiting Americans' exposure to China's market through government pension funds. They cited Beijing's restrictions on the release of some financial information and unusual influence over private companies.

Many investors view such a move by the US as mostly self-destructive, similar to how they react to any fear-mongering over China dumping its treasuries and causing a sharp spike in yields. The vastly integrated financial markets, in other words, are seen as the red line that neither country will want to cross in a long-lasting standoff.

China's further foray into dollar bonds only strengthens that thesis. For as much as the country throws its weight around, its financial system is simply nowhere near that of the US. The yuan is not a major foreign currency. Its bond market is comparatively underdeveloped and opaque, and, on top of that, S&P Global Markets predicts that onshore corporate-debt defaults will reach a record high in 2020. Relative to other developed-market economies, China lacks large institutional investors such as insurance companies and pension funds.

For those reasons, it is questionable to conclude that the US and China are truly in the "foothills of a cold war" that could morph into something worse than World War I, as Henry Kissinger described it earlier this month. For as far apart as the countries may seem on a range of issues, from trade to intellectual property and human rights, they are pretty much as close as ever in the financial markets. It is never a bad idea to follow the money.

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LETTERS TO THE EDITOR

Maha-politics

The denouement of the political drama in Maharashtra with more than the conventional five acts with each Act comprising a few scenes, watched in suspended disbelief, has given those of us who are opposed to BJP for what it represents and does in the guise of nationalism. Don't remind us that Shiva Sena too is essentially a Hindutva party, for it is relatively a small fry in the national canvas and it is willing to tone down its Hindutva stridency, and has agreed to go by what is called a common minimum programme. Further, any internal rift or internecine feuds within the Hindutva-oriented right wing makes it that much easier for the left-liberal forces to fight the divided Hindu right. The differences between BJP and Shiv Sena over power sharing and greater political space proved to be a blessing in disguise. BJP's failure 'to manufacture' a majority is a tribute to the moral strength shown by the MLAs of Shiv Sena, NCP and Congress. The incoming Uddhav Thackeray government goes to demonstrate that Narendra Modi-Amit Shah duo cannot have their way and satiate their greed for power all the time. The failed attempt at the usurpation of power must make them realize that Indian democracy is too big for them to bend it to their will and dissuade them from grabbing power by unfair means. It isn't enough to say that the Constitution is the Holy Book; one must live by it in letter and spirit.

— G David Milton, Maruthancode

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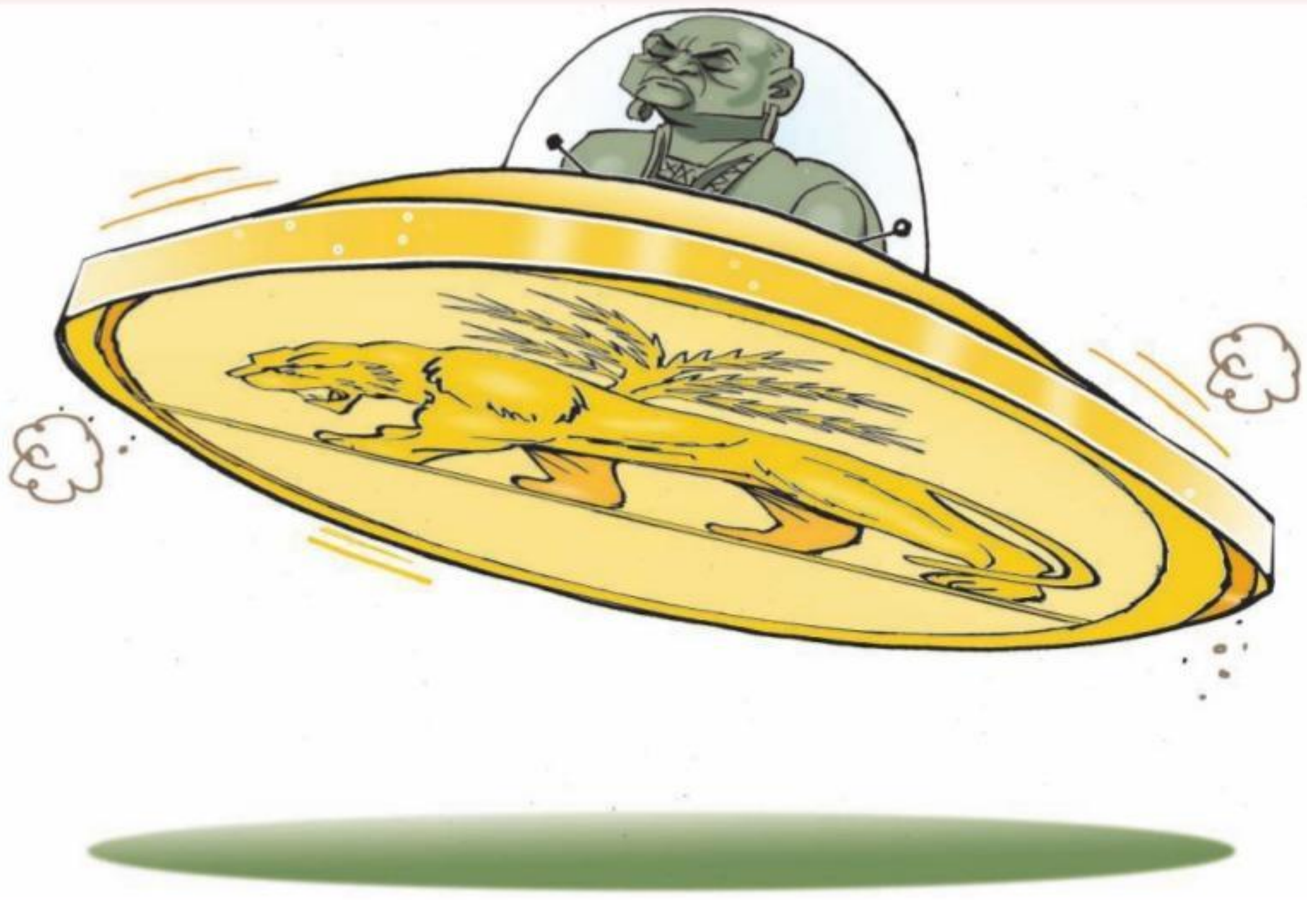

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Rethinking RBI's monetary easing policy

Instead of further rate cuts, RBI's focus needs to shift towards improving transmission efficiency and enacting broader banking-sector reforms—which facilitate greater competition amongst banks to ultimately move towards a repo-linked deposit and lending regime

THE LATEST INDEX of Industrial Production (IIP) and Consumer Price Index (CPI) numbers are likely to pose a serious dilemma for the Reserve Bank of India's Monetary Policy Committee (MPC), when it reviews key policy rates in its upcoming meeting on December 3-5. Based on credible signals of an economic slowdown, and RBI's stated position of an accommodative monetary policy stance in October, many analysts believe a further (repo) rate cut to be a foregone conclusion. The latest retail inflation numbers are likely to make it tricky.

The IIP numbers, released by the Central Statistical Organisation (CSO), showed that factory output declined sharply by 4.3% in September 2019—recording its worst performance in almost eight years, whether computed in the new (base year 2011-12) or the old (base year 2004-05) series. In the April-September period, the cumulative growth in industrial output was only 1.3%, compared to 5.2% in the same period a year ago. The latest decline is broad-based—with a substantial fall in the production of capital goods and consumer durables, and a slump in construction/infrastructure growth.

On the other hand, latest data from the National Statistical Office (NSO) showed that year-on-year CPI inflation was at a 16-month high of 4.62% in October, breaching RBI's medium-term target of 4% retail inflation. Notably, CPI inflation serves as the nominal anchor in the conduct of monetary policy under the current flexible inflation-targeting (FIT) framework of RBI.

Much will, of course, depend on second-quarter growth numbers, to be released on November 29. Estimates provided by the Japanese brokerage firm Nomura and SBI's Ecowrap report both project FY20 Q2 GDP growth at 4.2%, substantially lower than the officially reported Q1 GDP growth of 5% in the same fiscal.

The above numbers suggest that we are not only amidst an economic slowdown, but a full-fledged *stagflation* may potentially be on the horizon. This calls for a careful reflection on what might constitute an appropriate policy mix, including the monetary policy stance, under such circumstances.

In response to a significant economic slowdown, RBI has reduced repo rates five times on a trot—from 6.5% in December 2018 to 5.15% in October 2019—expecting that its transmission to lower interest rates will buttress credit uptake by firms, and kick-start an investment-driven growth cycle in the economy. While central banks in many countries have enacted monetary easing policy in response to the slowdown in domestic and global growth and uncertainties arising out of geopolitical tensions and trade wars, with a 135 bps reduction in repo rates over the past 10 months, RBI's stance has been the most aggressive among all.

> A weak supply-side and fiscal policy response to the slowdown has disproportionately raised the stakes for monetary policy to lose sight of its core objective of inflation management

However, in the emerging scenario of rising retail inflation in India, RBI's monetary easing policy requires a pause. Here's why.

The latest headline inflation numbers suggest that much of the rise in overall inflation has emanated from food price shocks, with substantial inflation observed in vegetable and pulses (26% and 11.7%, respectively) in October. Measured on a year-on-year basis, vegetable price inflation in urban and rural areas has been 35.4% and 21%, respectively. As surplus rainfall during August and September has severely damaged kharif crops across the key producing states of Rajasthan, Madhya Pradesh, Maharashtra, Gujarat and Karnataka, high food inflation is likely to persist.

The impact of such a supply shock is likely to feed into long-term inflation expectations, with the possibility of core inflation (currently at 3.47%) reverting to (the levels of) headline inflation. An IMF research* shows that, historically, the *pass-through* from headline to core inflation in India has been rapid—the gap reducing by three-fourths within one year due to significant second-round effects. The share of food in household consumption expenditure continues to be high (30% in 2017-18 as per the NSO). Research shows that high food inflation plays a critical role in informing both inflation expectations and wage-setting in India.

Currently, headline inflation has already breached RBI's medium-term target. RBI's September Households' Inflation Expectations Survey shows three-months and one-year ahead median inflation expectations have hardened to 8% and 8.1%, respectively. This implies that the central bank can ill-afford to lose sight of its core objective of maintaining price stability, a critical element of which entails anchoring long-run inflation expectations. Failure to do so can severely damage the credibility of the central bank, and question its commitment towards the FIT framework.

In addition, it is now clear that despite policy rate cuts, there has been a limited transmission to borrowing rates of corporates. Deposits constitute about four-fifths of total funds of banks, compelling them to offer high deposit rates, thus resulting in a low margin between deposit and lending rates. A reduction in repo rate does little to help the banks' overall costs of funds, leading to stickiness in lending rates. RBI's nudge to link retail loans to external benchmarks instead of internal ones based on marginal cost of funds can help improve this situation, but adoption by commercial banks has been predictably slow. In such a scenario, instead of further rate cuts, RBI's focus needs to shift towards improving transmission efficiency and enacting broader banking-sector reforms—which facilitate greater competition amongst banks to ultimately move towards a repo-linked deposit and lending regime.

The aggressive monetary easing policy of RBI is unlikely to boost investment demand in the economy unless aggregate consumption picks up. With the possibility of stagflation on the horizon, a right mix of fiscal, monetary and supply-side policies is required at this juncture. While the government needs to prioritise job creation and adopt expansionary fiscal policies to trigger a consumption-driven virtuous cycle of growth, RBI needs to focus on price stability. So far, a weak supply-side and fiscal policy response to the current slowdown has disproportionately raised the stakes for monetary policy to lose sight of its core objective of inflation management.

* 'Food Inflation in India: The Role for Monetary Policy', *by Rahul Anand, Ding Ding and Volodymyr Tulin*

DIVIDEND DISTRIBUTION TAX

Abolishing DDT is a bad idea

SHSHANK SAURAV

The author is a chartered accountant

It will not only impact tax collection, but will also affect investment cycle

IN SEPTEMBER, finance minister Nirmala Sitharaman announced a major tax cut for corporates, for which the estimated revenue loss is ₹1.45 trillion. Data released by the CBDT based on tax collection till September 2019 (after second instalment due date for advance tax) shows that income tax receipts increased by a mere 4.7% as against 17.5% projected in the Budget. This is worrying, because it doesn't include the impact of tax cuts that were announced after due date for paying second instalment of advance tax. There is a similar trend in indirect tax collection, where tax mobilisation has slowed down due to decline in consumption. The government is struggling to meet fiscal deficit targets amid growth slowdown, and cannot expect tax buoyancy in the coming period to improve the situation.

Indian corporates are now demanding to abolish the dividend distribution tax (DDT or CDT) on the pretext of double taxation. DDT is paid by a domestic company that declares dividend. It is necessary to understand the mechanism of taxation and the rationale behind imposing DDT before concluding it as double taxation for the taxpayer.

Section 115-O of the Income-tax Act, 1961, which casts an obligation on companies to pay DDT, has been amended, and provisions have been made beneficial to assesses. When DDT was introduced in the 1997 Budget, Section 10(34)—Section 10(33) at that time—was also inserted in the Act; it provided that dividend received by a person shall be exempt from taxation. DDT ensured due taxes are collected at source stage, notwithstanding the tax status of the person receiving such dividend. Taxability of dividend has changed; in the 2008 Budget, the government allowed domestic firms to offset the amount of dividend got from subsidiaries while computing DDT liability. The 2016 Budget took away some benefits enjoyed by taxpayers, and Section 10(34) of the Act was amended and the new Section 115BBDA inserted. From 2016, dividend income over ₹10 lakh is taxable at the rate of 10%. Few years ago, the government introduced tax on buyback of securities, when companies started taking share buyback route to avoid DDT.

> The govt provided major relief to the corporates by reducing tax rates; now, industry must respond positively

DDT was introduced to plough back the profit for investment and expansion. Gross fixed capital formation (GFCF) as percentage of GDP has declined from 34.1% in 2011-12 to 29% in 2017-18. There is a steep decline in gross capital formation (GCF) ratio also. The private sector has not announced any major investment after the recent corporate tax cut and, therefore, abolishing DDT at this point of time may prove to be counter-effective. Up to a certain extent, DDT restrains companies from distributing the retained surplus by way of taxation at the level of company itself, and undistributed profit is used by companies for expansion purpose. Abolishing DDT will not only impact tax collection, but will also affect investment cycle and, therefore, it makes no economic sense for such a move in the current scenario.

So far as double taxation is concerned, it must be appreciated that dividend income in the hands of small taxpayers is exempt from tax. Dividend income over ₹10 lakh in a year is taxed at a concessional rate of 10%. It may be argued that retained surplus belongs to shareholders of the company, and for all practical purposes DDT is in the nature of tax on shareholder's income that is withheld at source by the payer. The element of double taxation has been taken care of by allowing offset of dividend received from a subsidiary while determining DDT liability of parent entity. If there is double taxation in the entire chain, then it is on the person (other than company, charitable trust) who receives dividend over ₹10 lakh in a year. DDT ensures a shareholder having a large stake in a company doesn't go untaxed, and the threshold of ₹10 lakh covers only those people who have large portfolios.

The government has already provided major relief to the corporates by reducing tax rates, and now it is time for industry to respond positively and revive the investment cycle. Usually, public expenditure is increased in case of economic slowdown and, therefore, asking for another relief is unjustified, given that industry is yet to respond positively on the concessions that were given a few months ago.

India's idling growth engine

Measures announced by the government in recent months to jump-start the economy have not borne any fruit so far

ANUJ AGARWAL

The author is an economist. Views are personal

THE WORLD OF automobiles is ditching the internal combustion engine and is obsessing over electric powertrains. However, the analogy of an internal combustion engine and the Indian economy still remains very relevant. With growth faltering, it begs the question, which of the cylinders are firing that can keep the growth engine running?

The growth for the first quarter of fiscal 2020 came in at 5%. Private consumption—the most important cylinder of growth—took the biggest hit, and the high frequency data doesn't really give the confidence of consumption reviving soon. The NBFC crisis, which also dented private consumption, with financing companies less willing to lend, isn't likely to get resolved any time soon. A slew of corporate crisis further eats into the economic output and weakens the consumer confidence in terms of creating uncertainty about future economic prospects. The case in point being instances like the failure of PMC Bank and Jet Airways, and the critical condition in which India's leading telecom operators currently are. This puts jobs and incomes at risk. RBI's September 2019 survey shows that consumer confidence is at a six-year low, as sentiments around employment, income and discretionary spending declined.

Hopes are set on consumer demand to revive with RBI's easy money policy. But transmission of policy rate cuts at the retail level can do only so much to revive demand in an environment where sentiments remain weak. Even if the cost of money goes down, the consumer is unlikely to borrow and increase consumption, if future prospects of income and employment are not too comforting. A big push to rural demand is not really in sight. Income boost to farmers under PM-KISAN remains minimal. Moreover, much of the money allocated under the scheme remains unspent. Many states are yet to prepare and submit their database of farmers to make them eligible for the benefits. MSPs have witnessed a moderate increase this year. For many of the crops, *mandi* prices have remained even below the MSP. The recent untimely rains have further adversely affected farm output and incomes.

The investment cylinder looks weak as ever, and the expectations of capex revival just keep getting postponed with every forecast. Capacity utilisation levels remain low and below the optimal utilisation rates. In such a scenario, any new private investment is unlikely. Lower interest rates might only serve to encourage corporates to restructure their debts to reduce their debt servicing costs. Surveys have pointed to the fact that savings from reduction in corporate taxes aren't as huge as government estimates these to be, and there is no guarantee that these savings will translate into investment spending or increased payouts for employees. No business has an incentive to invest unless there is a visibility of increased demand and capacity utilisation. The CMIE Capex data, read as new and revived investments net of dropped, has remained mostly in the negative territory since the second quarter of fiscal 2018, barring a couple of marginally positive readings. Much of the onus of reviving investment, then, lies with the government, which remains constrained by fiscal considerations despite RBI's surplus reserve transfer, due to weak tax collections.

India has been long betting on exports to be its growth driver. The Make in India campaign is in the same spirit, without much success. In the current global scenario with rising protectionist sentiments and weak economic growth, even this cylinder fails to propel growth. Challenges on the external front have an adverse impact not just on India's exports, but also business sentiments and investments. While the IMF expects global economic growth to rise to 3.4% in 2020 from 3% in 2019, countries contributing to this acceleration remain fragile with greater downside risks.

The ongoing US-China trade war is having a detrimental impact on global economic growth and trade flows. Theoretically, the US-China trade war opens export opportunities for India via trade diversion. A recent UNCTAD study puts the trade diversion effects of the US-China trade war for the first half of 2019 at about $21 billion. India was able to capture only 3.6% of this. Competitiveness of Indian exports has always been questioned on account of inherent nature of our businesses and structure of supply chains, and government policies. India's decision to move away from the RCEP further isolates Indian businesses from the opportunity to be a part of the global value chain.

Growth revival remains crucially hinged on demand to pick up, which, in turn, is linked to sentiments. In a situation of weak sentiments, even a policy intervention like helicopter money can fail, where people might actually be inclined to hoard cash rather than spend it. Too much negative news flow further weakens the spirits. Emotional well-being and confidence is what drives discretionary spending—sentiments play the key role.

What will keep the growth revving at above 6% levels is difficult to say. A slew of measures announced by the government over the course of recent months to jump-start the economy have not borne any fruit so far, and will likely come into play only in the next fiscal. With recent economic data releases, analysts are pessimistic about the second quarter growth. SBI expects it to be 4.2%, and Nomura too is around the same levels. Both the banks are now expecting growth for the fiscal 2020 to be closer to 5%. One would wish for the economy to be similar to an electric vehicle, where you can get all the torque at once and pick up pace. Since it is not the case, it is time for the government to work its gears, send out the right signals, and get its growth cylinders firing.