INTERVIEW WITH VIJAY KELKAR & AJAY SHAH

'The middle-income trap can happen here'

IN THEIR recently released book, titled 'In Service of the Republic', VIJAY KELKAR (former chairman of the 13th Finance Commission) and AJAY SHAH (Professor at National Institute of Public Finance and Policy) lay out the reasons why India lost its growth momentum after 2011. The book also outlines how India can become a liberal democracy because if individual freedoms are not respected and state coercion not contained, even high growth will not be enough. UDIT MISRA spoke with the authors. Edited excerpts.

Vijay Kelkar and Ajay Shah. *Tashi Tobgyal*

You start off the book by saying that the book would try to answer why the reforms introduced from 1977 onwards delivered success during 1991-2011 period, but faltered thereafter. So what was the essential reason?

Vijay Kelkar: Simply put, under-developed institutions; weak institutional capacity.

Ajay Shah: Where did we go wrong? We had a slogan of becoming a market economy, of fostering economic freedom, of obtaining the economic dynamism that goes with these. But we did not think through what should be the role of the government in a market economy. It is not a matter of simple deregulation, of shutting down government intervention, as there are market failures in a market economy. There is actually a role for the state. We didn't do enough in thinking through the role of the state, on the problems of state capacity, on how to obtain competence in government organisations. And we failed to recognise the dangers of state power, of state coercion. How do you protect the private sector from state coercion? We didn't agree on an intellectual framework, and we did not build the institutional capacity to protect private persons in a market economy.

Given this argument against too much state intervention and not understanding the role of the state in a market economy, how do you look at the current growth deceleration in India, which has now gone from being the fastest-growing major economy to a major cause of concern in just 3-4 years? Was this expected? Are these the makings of India falling in the middle-income trap that you mention in the book?

Kelkar: We should not look at the 8 years after 2011. Changes in trend growth are long slow phenomena. Right from independence, our dream was that India should become a prosperous liberal democracy. But there are many instances in the international experience where this has not happened. That (middle-income trap) can happen here and that is why we started thinking about it. The most important word in this book is the 'republic': there is an intimate connection between the objective of liberal democracy and the objective of a prosperous market economy.

Shah: I want to say this in historical sequence. I was very excited about what was happening in India from 1991 onwards. But by 2006, 2007, which were the go-go years for the economy, I was starting to get extremely nervous about the decline in institutions. I was seeing vast sums of money being used by private persons to subvert state institutions. And I had a feeling that this would go badly. You cannot have a functioning capitalism without capabilities in state institutions. It took some time for the data to fall into place, but now the picture has become clear that 2011 was the year when that boom ended. In one data series after another, be it the growth rates of automobile industry or nominal private investments, there is a clear break and deceleration after 2011. So there was the 1991–2011 period and then there are the following eight years. The heart of this story is one of institutional decline.

What has prompted repeated governments to intervene so often? Is it a reflection of widening inequalities, or people's lack of trust in the market providing the solutions?

Shah: This book is not so much about here and now, rather the last 40 years and the next 40 years. With the benefit of hindsight, in the period after 1991, we the economists, the intellectual community, did not do enough in terms of thinking more deeply about the role of the state and the role of the market, understanding market failure, building a legal framework to bring in more checks and balances in the system.

For example, the SEBI Act was repeatedly amended during the 90s, but in those years we had little clarity about the difficulties of checks and balances in an agency, of firmly placing such an agency in a rule of law arrangement. These weaknesses of the analysis of that period are now coming back to bite us.

For full interview, visit www.indianexpress.com

FIFTH MEETING OF ECONOMIC ADVISORY COUNCIL

FinComm's final report to take note of GST stabilisation, revenue issues

ENS ECONOMIC BUREAU
NEW DELHI, DECEMBER 16

REPORT FOR 2020-21 SUBMITTED

- **The Commission last week submitted its report for the fiscal 2020-21 on devolution formula, which details how the Centre plans to share taxes with the states**
- **The Commission's Chairman NK Singh said that it has done modelling of 28 states with two new union territories of J&K and Ladakh in the 2020-21 report. It is expected to adopt the same approach in its report for the five-year period**
- **Monday's meeting discussed likely macro assumptions for the Commission's award period relating to real growth, inflation, tax revenues and expenditure patterns emerging both at the Union and states level**

THE FINAL report of the 15th Finance Commission for the five-year period will not be a "mechanical replication" of the report for 2020-21 that it submitted recently. The Commission may review its recommendations taking into account the structural reforms undertaken by the government, revenue and fiscal position of the Centre and implication of the goods and service tax (GST).

Speaking to reporters on Monday after the fifth meeting of the Economic Advisory Council of the 15th Finance Commission, its Chairman NK Singh said the report will be comprehensive and address wide ranging issues.

The meeting discussed likely macro assumptions for the Commission's award period relating to real growth, inflation, tax revenues and expenditure patterns emerging both at the Union and states level.

The Council also discussed issues related to stabilisation of GST, relationship between GST Council and Finance Commission and GST compensation being paid to states. At the meeting, some members suggested to have a look at the need for a cyclically adjusted fiscal deficit.

Singh said the Commission has done modelling of 28 states with two new union territories of Jammu & Kashmir and Ladakh in the 2020-21 report. It is expected to adopt the same approach in its report for the five-year period. As J&K and Ladakh are being treated as Union Territories, they would likely get share in grants and not share in tax devolution. He said the Commission intends to have a robust chapter on direct and indirect revenue issues.

The 15th Finance Commission was constituted by the President under Article 280 of the Constitution on November 27, 2017 to make recommendations for a five-year period from April 1, 2020 to March 31, 2025.

The Centre last month mandated the Commission to submit the report for fiscal 2020-21 by November 30, 2019 and then the final report for the period April 1, 2021 to March 31, 2026 by October 30, 2020.

The Commission last week submitted its report for the fiscal 2020-21 on devolution formula, which details how the central government plans to share taxes with the states. The award has not been made public as the formula is to be used in next year's Budget for deciding on sharing of taxes among the Centre and states.

As the government amended Article 370 of the Constitution, J&K was bifurcated into two Union Territories, Jammu & Kashmir and Ladakh.

There was a need to change Terms of Reference of the Finance Commission as J&K ceased to be a state.

'Outlook on residential real estate segment negative'

Citing subdued demand, slow sales, over-supply and liquidity crunch, rating agency ICRA has maintained a negative outlook for housing

UNSOLD INVENTORY MOSTLY IN PERIPHERAL AREAS: With most of unsold inventory comprising either units with high ticket sizes or units located in peripheral areas with weak network infrastructure, challenges associated with liquidation of stock are expected to continue

BETTER AFFORDABLE HOUSING SALES: Sales in the sub-₹50 lakh segment have gained momentum, and government incentives for development and offtake of affordable housing units along with both demand and supply for this segment will augur well

REASONS FOR MUTED PERFORMANCE OF HOUSING SEGMENT:
- Prevailing liquidity crunch
- High inventory overhang
- Weak affordability
- Subdued demand conditions

HEALTHY SALES FOR LARGER PLAYERS: Homebuyers are leaning towards reputed developers with established track record of on-time and quality project completion; thus, larger players are registering healthy sales

RELIEF DUE TO ₹25,000 CR FUND: Government measures such as the establishment of a ₹25,000 crore funds for stalled housing projects, may alleviate some of the execution or delivery-related issues going forward

Source: PTI

BRIEFLY

Date extended for filing advance tax for NE states

New Delhi: In view of the ongoing protest against the Citizenship Amendment Act, the Finance Ministry Monday said the CBDT has extended the last date to file advance income tax return to December 31 for north-eastern states.

Yamaha recalls 7,757 units of FZ FI, FZ-S FI

New Delhi: India Yamaha Motor (IYM) Monday said it is recalling 7,757 units of its FZ FI and FZ-S FI with immediate effect to rectify faulty rear side reflector.

Rupee settles 17p down at 71 against dollar

Mumbai: The rupee settled 17 paise down at 71.00 against the US dollar Monday, after rising crude oil prices and fag-end selling in domestic equities.

RCEP move 'to help vulnerable sectors'

New Delhi: India's stand not to join the Regional Comprehensive Economic Partnership (RCEP) deal will help vulnerable sectors, including dairy and farmers, who would have been "threatened" by the RCEP rules, the Commerce and Industry Ministry said Monday. **PTI**

Pradhan: Rural India to drive steel demand

New Delhi: Union Steel Minister Dharmendra Pradhan Monday, speaking at the 'Steeling India-2019: Driving metal intensity in key sectors' organised by CII, said steel demand growing in India, technology and innovation can make the Indian steel sector more vibrant.

Experts attend 'iLLUMINARE' conference

New Delhi: CEOs, general counsels and top management officials of various Indian and multinational entities attended the 'iLLUMINARE 2019' conference on December 13. Held at Trident Hotel, Gurgaon, it was organised by Anjamo Consulting, and attended by industry experts. **ENS**

Wholesale inflation rises in November

ENS ECONOMIC BUREAU
NEW DELHI, DECEMBER 16

THE OVERALL price level of wholesale goods rose 0.58 per cent in November as against 0.16 per cent in October on the back of a rise in food prices, shows data released by the Ministry of Commerce and Industry Monday.

After a slowdown in India's wholesale price index (WPI) inflation since June, this is the first month where the government has recorded an uptick.

Despite muted rise in prices of fuel and manufactured products, the country's WPI inflation has been impacted by sustained double-digit growth in commodities like food articles, vegetables and pulses as well as a continued spike in onion prices. The data comes nearly a week after the government recorded a three-year high in retail price inflation, which rose 5.54 per cent in November due to higher food prices.

Wholesale prices of food articles, which contribute to 15.26 per cent of the WPI, rose 11.08 per cent in November 2019 over the same month in the previous year. Milk prices, which makes up 4.44 per cent of the index, grew 1.60 per cent. Wholesale prices of onions, which makes up 0.16 per cent of the index, jumped 172.30 per cent, while vegetables, contributing to 1.87 of the WPI, also saw a 45.32 per cent spike in prices.

Prices of pulses, accounting for 0.64 per cent of the index, grew 16.59 per cent, while eggs, meat and fish, which make up 2.4 per cent, saw an 8.15 per cent rise in prices. At the same time, the price rise in non-food articles, which contribute around 4.12 per cent, slowed to 1.93 per cent from a 2.35 per cent rise recorded in October. Cereal prices, too, rose at a slower rate of 7.93 per cent in November compared with an 8.32 per cent rise recorded in October.

Manufactured food products, which account for 9.12 per cent of the index, also grew 5.05 per cent in November.

Apart from food items, other segments that witnessed a rise in prices include manufactured cement, lime and plaster and other manufactured transport equipment, which recorded a 5.24 per cent and 5.63 increase respectively.

"Due to the weak consumption demand the core inflation in November 2019 also remained benign and came in at -1.7 per cent, marking the fourth consecutive month of deflation," said Sinha. said Sunil Kumar Sinha, principal economist, India Ratings.

RIL, BP sign pact on fuel retail venture

ENS ECONOMIC BUREAU
MUMBAI, DECEMBER 16

UK OIL giant BP and Reliance Industries Ltd (RIL) on Monday signed a definitive agreement relating to the formation of their new Indian fuels and mobility joint venture (JV). This follows the initial heads of agreement signed in August this year. The JV is expected to be formed in the first half of 2020, subject to regulatory and other customary approvals.

"The new venture, a further development of RIL and BP's long-standing partnership, will include an India-wide fuels retail service station network and aviation fuel marketing business. Building from RIL's existing businesses, the partners expect the venture to co-create a world class fuels partnership to grow rapidly and help meet India's fast-growing demands for energy and mobility," RIL said in a statement.

The JV expects to expand from RIL's current fuel retailing network of over 1,400 retail sites and 30 aviation fuel stations across India to up to 5,500 retail sites and 45 aviation fuel stations over next five years. Castrol lubricants will also be available across the JV's network. The agreement was signed here by RIL CMD Mukesh Ambani and BP Group Chief Executive Bob Dudley. The partners intend to set up a new JV company, held 51 per cent by RIL and 49 per cent by BP.

Brookfield to invest in RIIHL

Mumbai: RIL on Monday said its wholly-owned subsidiary Reliance Industrial Investments and Holdings (RIIHL) has entered into binding agreements with Brookfield Infrastructure Partners, and its institutional partners, for an investment of Rs 25,215 crore in the units to be issued by Tower Infrastructure Trust. **FE**

Insolvency law to have positive impact on corporate bond market: Sebi chief

PRESS TRUST OF INDIA
NEW DELHI, DECEMBER 16

> **"IBC has ... successfully empowered creditors by increasing their recoveries, improved their debtor discipline..."**
>
> **AJAY TYAGI**
> CHAIRMAN, SEBI

SEBI CHAIRMAN Ajay Tyagi on Monday expressed hope that positive impact of the insolvency law will be visible on the domestic corporate bond market in five years. Describing the Insolvency and Bankruptcy Code (IBC) as a "landmark reform" in the country's economic history, Tyagi said the Code has brought in behavioural changes among corporate debtors. The Code came into force in December 2016.

"IBC has been a landmark reform that has successfully empowered creditors by increasing their recoveries, improved their debtor discipline... there is scope for further improvement," Tyagi said here.

According to him, reforms in bankruptcy laws leading to bolstering of creditor rights have generally been found to have a positive impact on corporate bond markets owing to increased investor confidence in the markets.

"In case of three BRICS countries — Brazil, Russia and China — the five-year average of outstanding corporate bonds to GDP ratio after implementation of bankruptcy reforms have nearly doubled compared to five-year average of outstanding corporate bonds to GDP ratio prior to implementation of the reforms.

"While there is a positive correlation between recovery rate, recovery timeline and corporate bonds to GDP ratio, experiences also show that there is a time lag between implementation of bankruptcy laws and effect on bond market to the extent of 5–10 years," he noted.

Considering that many financial service providers deal with substantial client firms and are or systematically important, "a separate, clear and appropriate resolution, bankruptcy and liquidation framework for financial service providers is the need of the day," Tyagi said.

He hoped that the FRDI (Financial Resolution and Deposit Insurance) Bill being contemplated will address this gap.

'Extension for Sabka Vishwas Scheme beyond Dec 31 unlikely'

PRESS TRUST OF INDIA
NEW DELHI, DECEMBER 16

THE FINANCE Ministry is unlikely to extend the last date for 'Sabka Vishwas Scheme', a dispute resolution-cum-amnesty scheme for settling pending disputes of service tax and central excise, which is ending on December 31.

Finance Minister Nirmala Sitharaman had unveiled the Sabka Vishwas (Legacy Dispute Resolution) Scheme, 2019, with the objective of settling pending disputes of Service Tax and Central Excise in the Budget. Live since September 1, the Sabka Vishwas Scheme provides a one-time window to eligible persons to declare their tax dues and pay the same in accordance with the provisions.

If anyone is interested to utilise the benefits of the Sabka Vishwas Scheme 2019, he or she must apply by December 31 as the last date will not be extended further, a senior Finance Ministry official said. So far, the scheme has attracted substantial attention and positive response, official said adding that 55,693 applications have been received with tax dispute amounting to Rs 29,557.3 crore as on date.

The CBIC has asked its principal chief commissioners to be more proactive in persuading eligible taxpayers to take benefit of the Sabka Vishwas Scheme.

PNB shares drop after under-reporting of NPAs

PRESS TRUST OF INDIA
NEW DELHI, DECEMBER 16

SHARES OF Punjab National Bank (PNB) on Monday pared early losses and closed marginally down after the Reserve Bank of India (RBI) said the state-owned lender under-reported its non-performing assets by Rs 2,617 crore for the last fiscal.

Shares of PNB dropped 0.85 per cent to close at Rs 63.90 on the BSE. Intra-day, the stock slumped 2.79 per cent to Rs 62.65.

The stock declined 1.01 per cent to settle at Rs 63.80 on the National Stock Exchange. During the day, it touched a low of Rs 62.60, down 2.87 per cent over previous close.

Over two crore shares of the state-owned lender were traded on the NSE, while more than 15 lakh shares exchanged hands on the BSE.

The public sector lender under-reported its non-performing assets (NPAs) by Rs 2,617 crore for the fiscal year 2018-19, as per RBI's risk-assessment report.

The divergence assessed by the RBI in net NPAs was also Rs 2,617 crore for the fiscal.

Also, the divergence in provisioning for bad loans in FY19 was to the tune of Rs 2,091 crore.

India well poised to attract investments that move out of China: Goyal

PRESS TRUST OF INDIA
MUMBAI, DECEMBER 16

COMMERCE AND Industry Minister Piyush Goyal on Monday said the country is well poised to attract investments that wish to move out of China.

Speaking at the India Economic Conclave 2019, he said the tax reforms introduced by the government recently will ensure investments come back to India.

"I think India is well poised to attract investments that wish to move out of China. We had a dialogue with a large number of companies. The income tax changes, which were approved by Parliament last week, are an important element in our plan to attract investments to and not let them go to any Southeast Asian countries which earlier offered attractive tax regime," he said. Goyal further said the government is also looking at pooling together land which state and central governments have got to offer.

'India should focus on bank clean-up, labour reforms to address slowdown'

LALIT K JHA
WASHINGTON, DECEMBER 16

WITH ECONOMIC growth slowing to a six-year low, IMF Chief Economist Gita Gopinath says the government should undertake structural reforms such as bank clean-up and labour reforms to address the slowdown in domestic demand. Gopinath, 48, who is travelling to India this week, rooted for government policies focusing on managing a slowdown in domestic demand, and on boosting productivity growth and supporting employment creation in the medium term.

"Given the cyclical position and the structural challenges of the Indian economy at this point, we recommend that policies focus on managing the slowdown in domestic demand, and on boosting productivity growth and supporting employment creation in the medium term," she told PTI in an interview.

Recommending a series of key policy priorities for the Prime Minister Narendra Modi government, she said, "Politically, the time — early in the government's second term — is right for a structural reform push."

GDP growth slowed for the sixth consecutive quarter in the July-September quarter to 4.5 per cent as manufacturing slumped on low domestic consumption.

Kolkata-born Gopinath said the policy priorities of the government should also include a credible fiscal consolidation path that is more ambitious than currently envisaged by the government.

"This is needed to reduce the high level of debt and reduce crowding out which would free up financial resources for private investment. This should be driven by subsidy-spending rationalisation and tax-base enhancing measures," Gopinath said.

Responding to a question, Gopinath said India's medium-term vision to reach a $5-trillion economy which focuses on boosting investment is appropriate. And so is the commitment to support the rural economy, boost infrastructure spending, streamline the goods and services tax (GST), direct tax reforms, and pursue a business-friendly policy agenda, she noted.

In this regard, Gopinath advocated, among others, three policy priorities for the Government of India.

First is to accelerate the clean-up of the banks, other financial institution, and corporate balance sheets and enhance governance of public sector banks to revive bank credit and enhance the efficiency of credit provision, while monitoring closely emerging risks from the liquidity stress in non-banking financial companies (NBFCs) and enhancing supervision and regulation of the NBFCs.

The Indian-American called for continued fiscal consolidation over the medium term — both at the Center and state levels — to lower elevated public debt levels, supported by further steps to increase tax compliance and administration, as well as improve fiscal transparency. **PTI**

'US-China deal, other developments to support global economic pick-up'

Washington: The announcement of a trade deal between the US and China that will de-escalate trade tensions, along with other developments like reduced likelihood of a no-deal Brexit, is likely to support a pick-up in the global economic activity in 2020, said IMF Chief Economist Gita Gopinath.

Global growth moderated to the lowest level since the global financial crisis this year, Gopinath said adding that this is an outcome of heightened trade and geopolitical tensions and country-specific factors in emerging markets.

In addition, advanced economies' growth is being weighed down by weak productivity growth and aging demographics. These factors lead to sharp weakness in manufacturing and trade almost across the globe, she added. **PTI**