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Yes, the rupee can appreciate more

Markets or currencies rarely move along a one-way street. In this world of new 'normals', going past gauges of overvaluation might just be a lost cause

WORLD MONEY

ABHEEK BARUA & BIDISHA GANGULY

Quite a bit of economics is unfortunately about zero-sum games. Portfolio investors in India clearly have reason to cheer but on the flip side exporters have reason to fret. A restrained current account and a flood of capital flows have trapped the rupee in a narrow range. Forecasters including ourselves are slowly reconciling to the prospect of medium-term rupee appreciation.

A number of things have happened to break the pattern of orderly depreciation of the Indian currency over the last couple of years. First, the dollar seems to be slipping into a phase of secular decline and that should mean gains for the rupee. The immediate trigger is the political uncertainty stemming from the Russia affair. However, there are perhaps bigger concerns about US economic policy. The inability to repeal Obamacare has revealed both a deep divide within the Republicans and the equally disturbing fact that while they are past masters at blocking legislation, they do not have concrete alternatives in place. Besides, the impasse over the health Bill has meant that other critical issues such as tax reform have been put on the back-burner. America is facing its own version of policy paralysis and this is hardly good news for the dollar. The widely cited dollar index, a weighted basket of exchange rates has seen a nine per cent drop from its peak.

From an economist's perspective though, there are other things that might cause more anxiety. After some traction in the first half, America's economic data is sagging again. Despite historically low unemployment rates (that should, in theory, push up wages and inflation) inflation remains below the US central bank or the Fed's target. Fed chair Janet Yellen's recent statement at a congressional testimony that the current policy interest of 1-1.25 per cent (the Fed funds rate) was close to the neutral rate — a sort of steady rate at which inflation is stable — came on the back of the weak data.

This could be interpreted in different ways. One clear implication is that Yellen and her team are unlikely to hike the rate from its current range of 1-1.25 per cent. Thus, the "pull" of rising American interest rates that could draw capital into the US is likely to be much more muted than earlier. In fact, with Europe picking up and emerging markets back in fashion, capital could flow out of the US. This could also corroborate the claim that America's trend growth rate is likely to be close to 2-2.5 per cent (the new normal if you like) rather than the aggressive three per cent that seemed to underpin Trump's budget plans. Thus, aggressive tax cuts or large expenditures run the risk of bloating the budget deficit and ramp up debt. These proposals are likely to be either rejected or heavily watered down by legislators.

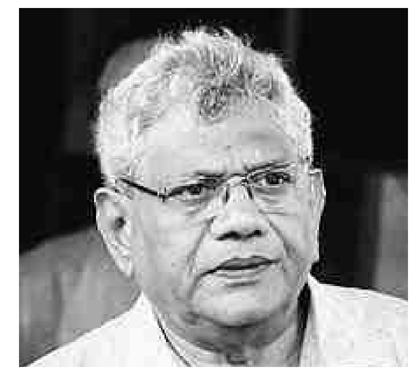
Shifting sentiment towards emerging markets has helped the stellar performance in India's asset markets and the run-up in the rupee. India is thus not an isolated case. In fact, if one looks a little far back, the Indian stock market has performed exactly in line with the MSCI emerging market (EM) index. Emerging market currencies are up this year and currencies such as the Malaysian ringgit and the South African rand have seen year-to-date gains similar to the rupee.

Part of the EM turnaround comes on the back of renewed confidence in China and there is growing consensus on the fact that an imminent economic crash is not likely. Thus, the Asian heavyweight is not just seeing a cyclical pop but a durable trend — a new normal again — of around seven per cent growth that will survive things like monetary tightening. Over 77 per cent of growth in the first quarter came from consumption spending, an indication perhaps that China's consumption-driven growth model is well entrenched. Finally, there is the new range for oil prices of between $45 and $50 a barrel that would support growth for net importers like India.

This is not to say that there won't be corrections in the future. Markets or currencies rarely move along a one-way street. The question is: How deep will they be? In this world of new "normals", going past gauges of overvaluation might just be a lost cause.

Abheek Barua is chief economist, HDFC Bank. Bidisha Ganguly is chief economist, CII

CHINESE WHISPERS



Cong sees red as Yechury loses out

Communist Party of India-Marxist (CPI-M) members of Parliament (MP), particularly those from Kerala, can be seen scurrying for cover when approached by members of other Opposition parties, particularly the Congress. Kerala MPs of the CPI-M are being pilloried because the state unit voted against a proposal to re-elect party General Secretary Sitaram Yechury (*pictured*) to the Rajya Sabha. Yechury was set to be re-elected from West Bengal with the support of the Congress, but the party faction closer to former general secretary Prakash Karat opposed the move. Opposition leaders — from the likes of former prime minister Manmohan Singh to former defence minister A K Antony and others — have told CPI-M leaders how they were "amazed" at the Kerala unit's decision. Some others have openly expressed surprise that the personal rivalry the Karats (Prakash Karat and his wife Brinda) have with Yechury should have contributed to such an important decision at a time when the Opposition is struggling to fight the Narendra Modi "juggernaut" and needed the services of the CPI-M chief in Parliament.

Demat or become invalid

The government and the Securities and Exchange Board of India (Sebi) have made dematerialisation of shares compulsory. While all new investors and companies issue shares in dematerialised format, some legacy investors continue to hold shares in the form of physical certificates. For years, Sebi and exchanges have been trying hard to achieve 100 per cent dematerialisation. Impressed by the government's demonetisation initiative, an exchange official recently offered a solution: "Like demonetisation, the government should declare all the shares held in physical form to be invalid after a particular date."

When son surpasses father

A number of messages circulating in social media are making fun of how the Central Depository Services has pipped its parent company Bombay Stock Exchange (BSE) in terms of stock performance. At a recent event when BSE Chairman Sudhakar Rao was asked the same question, he gave a father-and-son analogy. He said there was no better moment of pride for a father than to see his child prosper more than him.

Monetary Policy Committee: Credibility and consistency

The committee should take ground realities into consideration and choose the best way forward

SOUMYA KANTI GHOSH

Come August 2, the six-member Monetary Policy Committee (MPC) will announce its verdict. This is the sixth meeting of the committee and much water has flown under the bridge since the MPC came into existence. The good thing is that the fledgling MPC may be just settling down, with the committee members delivering a spilt verdict in June. However, there are still some thorns in the flesh as far as the MPC's operations are concerned.

Not many people are aware that the Reserve Bank of India (RBI) had published a research paper in 2007 on the operations of MPC across different countries. There were some remarkable findings regarding the literature survey of MPC operations in major countries. For example, in the surveyed literature it was found by the authors that there was no substantive case to argue committee decisions were better than more autocratic processes. It was also established that even as MPC promotes discussion and information sharing, it may also entail the risk of free riding. In fact, majority voting may even have weakened accountability besides reducing the informational efficiency of decision-making.

Notwithstanding such observations, the paper, however, concluded that the concept of MPC brings to the table diverse perspectives, independent thinking, technical expertise and pooling of analysis. The paper constructed an index of sufficiently empowered MPC on various parameters across countries and concluded that (between 2002 and 2006) more empowered MPCs seem to deliver better inflation results (level and volatility) but with no improvement in growth outcomes. Additionally, to accommodate the possibility of outlier countries impacting the group average (countries such as Brazil and Turkey have relatively more empowered MPCs but also a history of high inflation), the Index of MPC empowerment was also constructed excluding them.

We went a step further to validate whether the results hold post the financial crisis (*see table*). Interestingly, the result for the period 2009-15 changes as inflation volatility is surprisingly increasing with more MPC empowerment, but with no visible improvement in growth outcomes. If this is true, it clearly puts a question mark on the efficacy of MPC post the financial crisis. Does this mean the MPC failed to deliver on its avowed mandate of inflation targeting? We did some research on this and these were the results.

The success of inflation targeting is sometimes overemphasised. Between 2002 and 2008, inflation declined in most of the countries and this was mainly attributed to increase in information technology-engineered productivity. To validate the above, we analysed the productivity and Consumer Price Index (CPI) inflation data for inflation targeting countries. We found that in half of the 19 countries that we had studied there was structural break in total factor productivity after the adoption of inflation targeting regime. And post that structural break, productivity increased in 12 economies, of which nine exhibited a decline in CPI inflation in the post-break period compared to the pre-break period. Some food for thought for the MPC then?

EMPOWERMENT & MACRO PERFORMANCE (2009-15)

Index for MPC empowerment	Number of countries	Average inflation	CV of inflation	Average growth	CV of growth
0 to 5	8	3.38	0.49	3.90	0.52
6 to 10	12	2.85	1	2.32	1.97
0 to 5 excluding China & India	6	1.95	0.48	2.55	0.63
6 to 10 excluding Brazil & Turkey	10	2.03	1.16	2.23	2.04

Source: SBI Research

Let us now turn to some of the fundamental issues regarding the MPC. One of the common criticisms of the MPC is that if we take a look at the minutes of the Fed meetings these are more spontaneous and there is much more detailed discussion regarding the various aspects of the economy before arriving at the conclusion. But the MPC discussions in the Indian context seem to be more structured and sometimes the consistency in arguments seems to be time-varying. With the progress of time, we hope such discussions will become more nuanced, spontaneous, lively and backed by members' own forecast and not purely by the professional forecasters' data as published by the RBI.

The most compelling observations regarding the various facets of MPC operations is, however, by Alan Blinder (2008). Blinder was the vice-chairman of the Board of Governors from 1994 and served till 1996 and was known for his plainspeak and critical appraisals. One of the most important remarks of Blinder was regarding the composition of the MPC. He was rather forthcoming in saying that contrary to popular perceptions that monetary policymaking should always be made by outstanding technocrats (Ben Bernanke, Stanley Fischer etc), only having outstanding PhD macroeconomists on the MPC was not a pareto optimal solution. Blinder also mentioned that members of the Federal Open Markets Committee and the European Central Bank Governing Council were mostly career central bankers (read market practitioners in the Indian context) that contributed to the MPC success.

In fact, concentrating on accomplished research economists would have meant Paul Volcker (an outstanding government official) and Alan Greenspan (a business economist) not sitting on the MPC. To quote Blinder: "My own experience on the Federal Reserve Board taught me that it is useful to have colleagues with more experience in banking, and in financial business in general, than academics normally have — even if these colleagues don't understand linear quadratic models. I don't necessarily believe that publishing a lot of notable scholarly work on monetary economics is the best possible credential for a central banker."

Some of these observations may find echo in the Indian context.

The MPC has been entrusted with the onerous job of setting rates in the Indian context and to be fair, we should give it time to get accustomed to the enormous cynicism and glare in the public domain. But it is also expected that the MPC takes into cognisance the ground realities and makes decisions accordingly. The spilt verdict in June hopefully will set the ball rolling for more diverse discussions on a going-forward basis? Will it be 6-0, 5-1 or 4-2 on August 2? My bet is the odds of a rate decision (preferably cut than hold) this time could be 4-2. Let's wait till then.

The author is group chief economic advisor, State Bank of India. The views are personal

BUSINESS LIFE

Things you are doing wrong when eating ramen

A few rules of thumb are necessary to tackle this unwieldy food

KET KRADER

For fans, ramen is a thing of beauty, taut noodles in a steaming rich broth, ready for instant consumption.

Yet devouring a bowl of ramen can be... daunting. Few foods inspire such a cult-like following, and yet it's kind of unwieldy to eat. Do you slurp up the long noodles, or attempt to "cut" them up with your chopsticks? Do you copy the guy that picked up his bowl and drank from it, or has he just never been to a restaurant before?

For some general rules of thumb, we turned to Ivan Orkin, founder of Ivan Ramen, which has two locations in New York. Orkin, a white guy from New York state and a star of Season 3 on *Chef's Table*, started his ramen career in Tokyo by watching experts cook; he caused a sensation when he opened his own shop in the Japanese capital.

Orkin has spent years studying the art of ramen and knows exactly what — and what not to do — with your precious bowl of noodles. Here are his rules, in his own words.

■ You're letting it get cold: The first rule of ramen is to eat it while it's hot. No smart person would push aside a fresh-from-the-oven pizza to start eating salad, right? The majority of ramen arrives with a hot broth, which means noodles can overcook if they sit for too long.

■ You're battling your noodles: When a bowl of ramen is placed in front of you, the noodles will probably be coiled together. If you take a moment to untangle them with your chopsticks, pulling them out of the coil, they're easier to eat. If you just grab a large section of the tangle, the noodles will flight you back — they'll all come along, and then you can't fit the bite into your mouth.

Ivan Orkin adds toppings of various ingredients to a bowl of ramen at Ivan Ramen in Tokyo. He is the founder of Ivan Ramen, which has two locations in New York PHOTO: BLOOMBERG

■ You're not slurping: Do not be afraid to slurp your ramen. In Japan, it's expected. For one thing, it cools hot noodles down. Noodles you can slurp are also the sign of a broth with enough fat to cling to them. If you can't slurp — if the noodle feels dry — the broth isn't rich enough.

■ You're biting off more than you can chew: A lot of people make the mistake of grabbing a giant pile of noodles that they can't really handle. Rule of thumb: Take a smaller amount than you think you want. You do not want to be sucking noodles into your mouth and then biting them in half so that some falls back into the bowl. Plan for a full — but not overwhelming — mouthful of noodles.

■ You're not paying attention: I like to think of ramen preparation as an action sport, an interactive activity. If you're lucky enough to sit at a ramen bar that overlooks the kitchen, watch them build the bowl. It's a surprisingly complex procedure for something that seems so simple.

■ You're not taking toppings seriously: When I go to a ramen shop for the first time, I choose the bowl that the place is most famous for. I will go easy on the toppings. I want to know if I like the flavour of the ramen and what the fuss is all about. If I go back, then I see if they have a special, and that's when I experiment with toppings.

■ You're ignoring your beverage: Be ready to drink a tremendous amount of water with your ramen. Or beer. Or both. There's a lot of salt in the broth, whether you know it or not, and if you don't drink water, you are going to feel crappy, I guarantee it. In Japan, they sell a special black oolong tea that helps you digest the pork fat in tonkotsu ramen.

■ You're minding your manners too much: It's okay to drink the broth from the bowl. It's considered a compliment to how good the broth is. But finish it at your own risk; those broths are flavour bombs, packed with sodium. Another thing that is okay to do is to ask for extra noodles if you've finished the ones in your bowl. Last, have a stack of napkins handy, ramen can be a bit of a mess. That's why ramen is so popular.

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LETTERS

What sells in politics

With reference to Shekhar Gupta's article, "*Hamara desh badal gaya hai*" (July 29), when Atal Bihari Vajpayee was facing an election in 2004 during his second term as prime minister, no one thought the Bharatiya Janata Party (BJP) would be defeated despite the "Indian Shining" campaign and its good, visible impact. That means one can never take Indian voters for granted.

So, should the BJP assume that it will come to power in 2019 and Narendra Modi again become prime minister even though the BJP has become strong in the recent past? Of course, Modi and BJP President Amit Shah are master strategists; they are working meticulously to ensure the party spreads its footprint throughout the country and the Opposition's power gets diminished.

I agree with the writer that voters today are smart enough to ask politicians the right questions and have expectations from them. They consider it a positive thing when politicians take a tough stand against corruption and walk the talk. People were hassled for months due to demonetisation but they still supported it.

What Nitish Kumar did might be called defection, betrayal, opportunism or something else, but he knows what sells and what does not in the political arena of India today.

Bal Govind Noida

Opposite view

With reference to the editorial, "Privacy by choice" (July 28), there is an imminent need for a clear stand by the government on the issue of citizens' right to privacy. It's strange that the Attorney General thought it wise to express polar opposite views in two different cases in the Supreme Court on whether right to privacy is a fundamental right.

He tried to justify his inconsistent stand by arguing that "even if it (right to privacy) is assumed to be a fundamental right, it is multifaceted". Can he take such a polar opposite stand to "suit" the government, more so when the matter is being considered actively by the Supreme Court?

I endorse the editorial's observation that the state is "overreaching" its authority by making Aadhaar mandatory for filing tax returns. The top court has already ruled that Aadhaar should not be compulsory for any purpose other than when the government is offering special benefits under its various welfare schemes.

The government shows scant respect for that ruling and has been trying to "universalise" the use of Aadhaar among citizens. Why such a haste? The government should wait for the final outcome of the petition concerning the right to privacy of citizens, which is being heard by a bench of the Supreme Court.

Right to privacy must be preserved. For the present though, our hopes are pinned on the Supreme Court.

S Kumar New Delhi

Self-regulation is key

With reference to Anup Roy's report, "Reserve Bank extends 'rest' period for auditors to 6 years" (July 28), the grounds on which this decision was taken are justified. They are also suggestive of the unethical practices being followed by professionals and banks alike.

Regulatory oversight alone cannot ensure best practices of governance in organisations that manage huge resources including public funds. Diminishing public trust in professionals is a matter of worry not only for the government or regulators, but also for the citizen and taxpayer. Even the possibility of lateral movement of individuals from one chartered accounting (CA) firm to another can reduce the impact of forced "rest" periods.

The only option is self-regulation by professional bodies. The institute of CAs, the Reserve Bank of India and banks should expose unethical approaches by individual firms and their employees. If proven guilty, the firms/individuals in question should be punished. If there are legal hurdles, the government needs to step in.

M G Warrier Mumbai

Letters can be mailed, faxed or e-mailed to:
The Editor, Business Standard
Nehru House, 4 Bahadur Shah Zafar Marg
New Delhi 110 002
Fax: (011) 23720201 · E-mail: letters@bsmail.in
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HAMBONE

BY MIKE FLANAGAN

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More hype than substance

Markets' dizzy heights point to short-term blips

The Nifty created history last week by moving past 10,000 on the back of concerted buying from every class of investor. Foreign portfolio investors (FPIs) continue to be attracted to the story of an economy that is undertaking reforms such as the goods and services tax (GST) and the new bankruptcy law. Domestic institutional investors (DIIs) have pumped money into equity. While the DIIs have bought a substantial ₹48,101 crore between July 1, 2016, and June 30, 2017, and the FPIs have invested nearly ₹55,000 crore during the same period, their enthusiasm has been dwarfed by that of retail investors. There has been a surge in the allocation of household savings to equity. Mutual fund folios have grown by 9.3 million in the last 12 months, rising to a record 58.2 million folios by end-June 2017. There are more than 14.5 million active Systematic Investment Plans (SIPs) and Equity Assets Under Management (including assets under management of equity funds, equity-linked savings schemes, and exchange-traded funds) have risen by ₹1.9 lakh crore. Retail investors have directly invested even more. A recent survey of 300,000 individuals indicates that 84 per cent of investors directly buy equity while only 59 per cent invest via mutual funds.

There are several reasons for the rising retail interest. For one, other asset classes appear unattractive. Falling interest rates have meant lower returns from debt; gold is suffering from low global prices, and the real estate market has slowed due to demonetisation. As the consumption story has also taken a break after demonetisation, households have deployed their savings in equity. Most importantly, there has been a positive feedback loop as well. The Nifty has shot up by over 16 per cent in the last 12 months as money has flooded in. Midcaps have done even better with the Midcap Index up by a stunning 32 per cent. Inevitably, capital gains have created a wealth effect and even more retail savings are finding their way into the stock market in the hope of quick returns.

However, this bull run has been based more on hope and hype than on fundamentals. Earnings have not grown at a commensurate pace. The last two quarters saw a slowdown due to demonetisation. The GST will also have a disruptive impact, which means that earnings growth may take a while to accelerate. Valuations are at alarmingly high levels, with the Nifty trading at a price-earning (PE) ratio of 25-plus and the Midcaps trading at over 35 PE, giving rise to concerns of an equity bubble. While the GST should lead to eventual gains, the initial impact is likely to be negative.

Indeed, analysts tracking key sectors such as automobiles and fast-moving consumer goods (FMCG) have issued warnings about the negative trends on profitability in the short term. One of the cornerstones of prudent investing is to divide assets across multiple classes. This ensures there is no over-dependence on any one asset class. At the moment, the retail investor is heavily overweight in equity and, therefore, very vulnerable to a setback in stock markets. Prudent investors should consider reducing their equity exposure and reshuffling portfolios, in order to deploy more resources to other assets. Otherwise, the next bear market could take the savings of many households down with it.

Pakistan's known unknowns

India needs to brace itself for more turmoil

The truism, that in Pakistan the only certainty is uncertainty, has been proved yet again after Nawaz Sharif stepped down as prime minister last week. Mr Sharif prematurely ended a third stint after the Supreme Court disqualified him on corruption charges linked to Panama Papers revelations involving his children. With his brother and chief minister of Punjab, Shehbaz Sharif, tipped to take charge after 45 to 55 days, within which he will have to contest a by-election to the National Assembly from the seat vacated by his brother, the political situation is unlikely to change dramatically in Pakistan. Thus, the Indian security and foreign policy establishments, preoccupied with developments on the Sikkim-Bhutan border, may draw reassurance from the fact that the Sharif family and its party, the Pakistan Muslim League – Nawaz (PML-N), remains in charge. It is, however, axiomatic that these political arrangements are unlikely to enhance the cause of stability in the region, not least because the run-up to the elections, due mid-2018, will witness an escalation of the traditional political contestation between the civilian and military establishments.

The immediate impact could be an upping of the ante along the Jammu & Kashmir border, the Pakistani military technique for tapping popular anti-Indian sentiments. But the months ahead could determine the survival of Pakistan's fragile democracy. The year 2013 saw for the first time the peaceful handover of power between civilian governments in Pakistan. Today, the PML-N has a popular mandate — it commands 189 seats in the 342-member National Assembly and brute majorities in the Punjab Provincial Assembly, the largest and most powerful of the provinces, and the J&K Assembly in Pakistan-occupied Kashmir. But corruption allegations have significantly weakened Mr Sharif's championship of the virtues of civilian government. True, his disqualification was made on somewhat weak grounds that he had not declared directorship of a UAE-based company in electoral filings, violating office-of-profit strictures (Mr Sharif claims the case did not arise as he did not receive any income from the company). But on the wider accusations of questionable realty deals involving, chiefly, his daughter and political heir Maryam, he is on weak ground.

It is worth noting that the Supreme Court has referred all cases to the National Accountability Bureau, the chief anti-corruption body, which has set up a joint investigation team. Significantly, the latter will comprise representatives of the ISI and military intelligence. Mr Sharif's relations with the military reached a new low in recent months after a newspaper published a report claiming a rift between civilian and military leaders over fighting militancy. The army suspected Mr Sharif's government leaked the story and tweeted its dissatisfaction with his attempts to make amends by firing a minister.

These ambiguities bring into play former cricketer Imran Khan's Pakistan Tehreek-e-Insaf (PTI) party, which spearheaded the campaign against Mr Sharif and is known to be propped up by the ISI-military complex. The PTI has been gaining traction among middle-class Pakistanis for its anti-corruption, aam aadmi credo, a contrast to such traditional feudal powers as Mr Sharif represents. As things stand, the choices for Pakistan lie between a precarious civilian government and a resurgent military, which has been unwilling to see its influence challenged.

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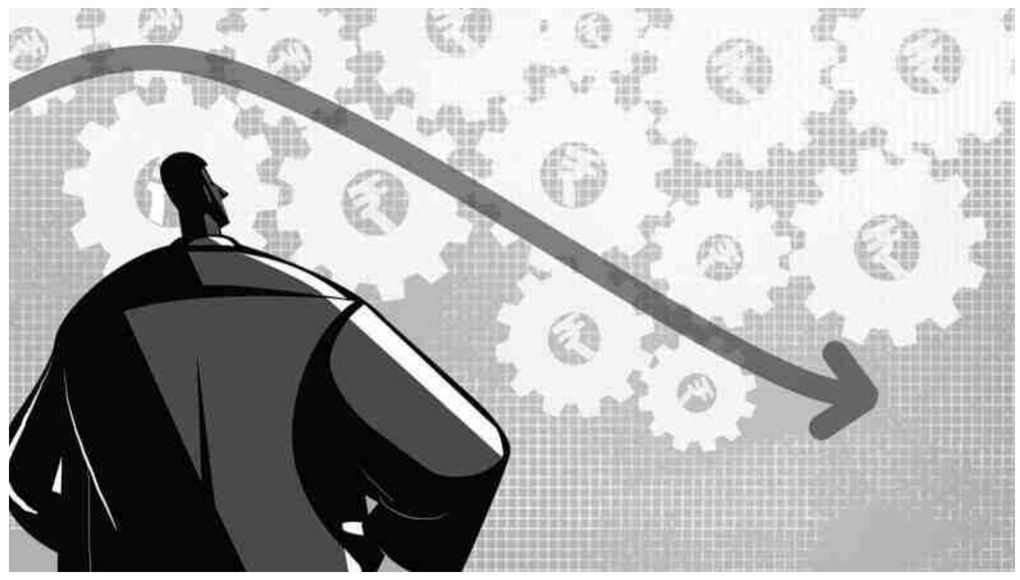

A government that takes jobs away

Govt inaction is preventing job creation; its actions may have led to job losses

POLICY RULES

MIHIR S SHARMA

It has been over two months since the last official growth data were made available. That print showed that gross value added at basic prices had consistently slowed from January-March 2016 to January-March 2017: From 8.7 per cent to 7.6 per cent to 6.8 per cent and finally to 5.7 per cent. This column pointed out at the time that the economy had begun to revive prior to 2014, but a new slowdown has begun under Prime Minister Narendra Modi's watch — the 'Modi Slowdown', as it were.

It is unfortunate that, in the two months since these numbers, there has been no significant sign that the government is working with new energy to resurrect the economy. It is true that much of the finance ministry at least will be understandably distracted by the roll-out of the goods and services tax. But it is far from clear why there continues to be no movement on more fundamental reform. The winning over of Bihar's Nitish Kumar to the National Democratic Alliance only reveals with greater clarity the vast difference between the political audacity and policy timidity of this government. It is all very well to say that fundamental reforms, such as to labour laws, are being left to the states to conduct; but when you rule practically every state in the north, west, and northeast, that argument gets shown up as the weak excuse for inaction that it always was.

The question that must be asked is: Why does the government feel no political pressure to move swiftly on reform before it faces the electorate in 2019? There can be multiple explanations. It could be that the ruling party is simply confident that there is no possibility that the Opposition can take advantage of the subpar economic performance and regroup in time for 2019. But Mr Modi and Amit Shah do not come across as the overconfident sort, and so this theory should be dismissed. It could be that they genuinely think they have fulfilled the promises that they made in 2014; but let us give them credit for enough intelligence to see through that claim, even if they wish to gamely try and sell it to others.

Is it, perhaps, that they simply do not believe that the impact of their economic management is as worrying as the GDP numbers suggest? After all, they may argue that the human cost of those lost percentage points of growth is not immediately obvious; these costs may not be politically relevant. But that surely cannot be the case. The actual, on-the-ground costs may be hard to calibrate in the absence of high-frequency, high-quality job creation indices, but there are an increasing number of replacements for this lack. One, exclusively discussed on the pages of *Business Standard*, is the result of an extensive household survey conducted by the Centre for Monitoring the Indian Economy.

The results of this survey, detailed by Mahesh Vyas of CMIE in a series of columns in these pages, have been disturbing. Here are some points made by Mr Vyas, based on the survey, just last fortnight ('Replace informal occupations with formal ones', *Business Standard*, July 17):

- "Between September-December 2016 and January-April 2017, while the number of farmers who owned land increased by 3.7 million, the number of agricultural labourers declined by 5.6 million."
- "The number of daily wage earners (non-agricultural) dropped by five million during the same period... In the earlier surveys we saw their numbers grow by about 9.5 million."
- "During January-April 2016, there were 93 million such [formal] jobs. This fell to 89 million in May-August 2016 and then to 86 million in September-December 2016. They remained at 86 million in January-April 2017. Compared to a year ago, these formal jobs have fallen by about 7 million."

Put together, this is a disquieting set of numbers. Certainly, the impact of demonetisation on the informal economy is visible in the survey. The number of daily wage earners and agricultural labourers together declined by 10.6 million. But this does not mean that the economy is creating formal jobs to compensate. In fact, such jobs have actually fallen by seven million over a year if the CMIE is to be believed. Note that this process was in motion before demonetisation occurred; the coincidence with the slowdown in growth in the official data must be noted.

This combination of facts suggests very strongly that the past 18 months have seen considerable grassroots distress as a consequence of a failure to sustain economic growth. The government has very few excuses for its inability to do so. Unlike the UPA, it has faced no global economic crisis, it has faced only helpfully low commodity and fuel prices, it has had no "taper tantrum" to deal with, there is a considerable pool of available global capital, and global demand has been slowly reviving.

Seen with cold objectivity, this result under benign circumstances would suggest the Modi government has been one of the most incompetent economic managers of the Indian economy in recent decades. More charitably, it could be said that it has moved too slowly on structural, administrative and financial reform. Even basic "tough" administrative decisions, such as those required to deal with indebtedness and bad loans, have taken too long. Its focus on infrastructure is welcome, but in the absence of competiveness-enhancing structural reform, new infrastructure will simply not create larger businesses and jobs.

The government thus has no choice but to accept that its actions have not just failed to create new jobs, but likely led to actual job losses. Needless to say, this is the opposite of what it promised in 2014. I do not recall Mr Modi vowing to take voters' jobs away.

Some may hope to ride out the discontent that this failure has surely created because of the absence of an effective opposition. But that is never wise in any case — opposition can emerge from anywhere if discontent is real. Perhaps it intends simply to divert the national conversation completely away from economic aspirations towards social issues. This, if cynically productive politically, would be unfortunate for India's future. If these are not its plans, then it is time for some hard thinking and harder decisions. The government must realise that it has very little time to recover itself, its reputation, its legacy — and India's fortunes.

m.s.sharma@gmail.com
Twitter: @mihirssharma

Toilet mystery: Blaming and shaming not the way

DOWN TO EARTH

SUNITA NARAIN

What makes people change their behaviour? Is it education? Is it the availability of options? Is it societal pressure? Is it the fear of penalties? Or is it all of these and more? This is a zillion-dollar question for policymakers trying to curb climate change or stop open defecation.

Take the matter of toilets. Getting people to build and use them is turning out to be the biggest conundrum. Mahatma Gandhi had said that sanitation is more important than independence. Lack of sanitation is leading to avoidable deaths of infants, and underweight and stunted children. This is unacceptable.

The good news is that the government of India has set itself an ambitious goal to end open defecation in the country by October 2, 2019, Gandhi's 150th birth anniversary. After many years of unsuccessful toilet-building programmes, the government has accepted that its goal is not to build toilets, but to increase their usage. In other words, people have to change their behaviour and begin using toilets. In fact, the government now wants to count usage and not toilets in its surveys. This is not a small change.

Report after report has shown that toilets are built, but not used. The 2015 report of the Comptroller and Auditor General had found that 20 per cent of the toilets built under government programmes remained locked or were being used as storerooms. In 2015 again, the National Sample Survey Office (NSSO) recorded the use of toilets in 75,000 households in 75 districts. The results were stark. In a few states, including Sikkim, Kerala, and Himachal Pradesh, 90-100 per cent of the toilets built were in use. But in many states the usage was low. In economically poor Jharkhand, it was below 20 per cent. Even in progressive, more literate and relatively rich Tamil Nadu, toilet usage was just 39 per cent.

How, then, will usage increase? What will drive the change in behaviour? This is not an idle sociological question. It is about the politics of development.

My colleagues, who investigated this, have found that state governments, pushed by the ambitious and much-needed targets set to make India open-defecation-free, are using name-and-shame as one way to bring about this change. They are pushing towards making open defecation socially unacceptable. Haryana (a successful state in terms of toilet usage), Uttar Pradesh (a dismal failure), Madhya Pradesh, Chhattisgarh, and a few other states have passed bills making it compulsory for anyone contesting panchayat elections to have a functional toilet at home. Many districts are taking this approach forward by blowing whistles at people defecating in the open, publishing their photographs on village billboards, cancelling their ration cards, or taking away other government benefits.

In Rajasthan's Pratapgarh district, this aggressive drive has had tragic consequences. Women defecating in the open were being photographed by government officials. There was protest and one man died. When my colleagues visited Mehtab Shah Kachhi Basti — literally meaning the illegal settlement — they found that women had little option but to defecate in the open. One, they are poor. Two, they have no real home to call their own; they have no land on which they can build a toilet. Three, they have no running water. Even the community toilet is inadequate to cater for the 3,000 people living there. Worse, its upkeep is pathetic and it has no water.

But this does not fully explain the habit of open defecation. After all, people buy mobile phones or bicycles before they invest in toilets. So, what will create the demand for toilets?

I believe this issue needs to be discussed openly and much more furiously. It is critical to invest in the software of behaviour change. This means doing a lot more to build awareness about the health impacts of poor sanitation. My own research shows that this link is known only in terms of policy; not in terms of actual data, which will build health awareness to drive behavioural change. Tobacco is one case where behaviours have changed. This is because there is no longer any doubt about the ill-effects of tobacco. We need the same with toilets.

Today, the government's Swachh Bharat Mission accepts this and even provides money for what in officialese is called intensive IEC (information, education and communication). But its own data show that in 2016-17, the government spent 0.8 per cent of its allocation for IEC, against the 8 per cent it had provided in its guidelines.

It is clear subsidising toilet construction is not enough. Much more needs to be done in terms of incentives that make people change their behaviour. In places like Mehtab Shah Kachhi Basti, the government will have to provide options for affordable community toilets that are clean and well-maintained. This also means recognising the crucial connection between water and toilets.

However, we still need deterrence. There is no doubt that societal pressure works. But we have to make sure that we do not end up blaming or shaming the victim. This is not the way to a cleaner India, but only a more ashamed India.

The writer is at the Centre for Science and Environment
sunita@cseindia.org
Twitter: @sunitanar

The destruction of equality

BOOK REVIEW

ROBERT B REICH

The greatest threat to Western liberal democracies in the future is more likely to come from extreme inequality than from Islamic extremism. This is because inequality erodes two foundation stones of modern society — openness to new ideas and opportunities, and a conviction that all citizens are morally equal.

For the first three decades after World War II, openness and equality constituted a virtuous circle. Openness generated unprecedented levels of prosperity. That prosperity allowed America and the citizens of other modern nations to invest in excellent schools and universities, basic research, modern infrastructure and social insurance. These investments, in turn, made it easier for people to adapt to change, and fostered ever greater equalities of income and opportunity. The result was a high level of trust in the fairness of the political and economic system.

But by the 1980s, the virtuous circle had stopped working. Economic and technological dynamism was upending jobs, convulsing communities and splintering families. At the same time, inequalities of earnings, wealth and job security were widening. After the financial crisis of 2008, many Americans, along with the citizens of other nations affected by the crisis, began to doubt the fairness of the system.

Two important new books offer useful and complementary explanations for what has occurred and, by implication, what must be done. In *The Fate of the West*, Bill Emmott argues that the 2008 financial crisis and its aftermath resulted from "a devastating blend of complacency, negligence and corruption" in the years leading up to it. The banks that created the calamity got bailed out and no top executive went to jail, but millions of people lost their jobs, savings and homes. Nearly a decade later, many citizens in the United States, Britain, France, Italy and elsewhere still feel trapped in dead-end jobs or don't have jobs at all. The result has been a profound loss of confidence in the system.

Emmott, who was editor in chief of *The Economist* from 1993 to 2006, faults economic and political elites who chose to advance themselves at the expense of the larger society. He points to a paradox deep within modern capitalism: The same financial incentives that spur innovation and investment can also lead the captains of industry and finance to manipulate the rules of the game for their own benefit, and thereby harm those without power. These moneyed elites "are the true sources of the sense of inequality that is currently threatening the openness that has enabled us in the West to flourish," he writes. "They are the explanation for Trump, for Brexit, for Le Pen."

Emmott argues that the financial interests of banks and big companies have distorted and disarmed public policy. Both of America's political parties are culpable. "Most notorious, in the US at least, was the successful lobbying in 1998 by Wall Street of the treasury secretary, Robert Rubin, and his deputy, Larry Summers, to block regulation of the trading of complex derivatives products which had been proposed by the then head of the Commodity Futures Trading Commission, Brooksley Born." Emmott also criticises big companies like Google, which have the lobbying and financial heft to get whatever they want in Washington. Campaign finance scandals have likewise revealed the political influence of money in Germany, Japan, France, Britain and elsewhere.

Emmott sees political and civic equality as the means to an open society. But why shouldn't such equality be an end in itself? In "One Another's Equals: The Basis of Human Equality," Jeremy Waldron, a professor of philosophy at New York University School of Law, argues that Western thought has been rooted in the moral imperative that people be treated and respected as equals, whatever disparities may exist between them in wealth or talent. Waldron sees moral equality between human beings as what's left over when "merit" is set aside. People deserve equal concern and respect because they are humans. Differences in wealth and power are consistent with this imperative if those differences serve the interests of all. Thus the answer to whose good is to be promoted in our social arrangements is — everyone's good.

Waldron warns that wide inequalities of income and wealth can erode this moral imperative because they make it harder to make the mental leap it requires: The poor may come to seem so different from the privileged and prosperous that the well-off cannot understand a moral principle that assigns equal value to the living of a human life as such.

Waldron urges the same sort of political equality as does Emmott, but he gets there from the opposite direction. For him, the purpose of political equality is not to preserve an open society. It is to honour basic human equality. "It is because we are one another's equals that we ought to have concern about high levels of economic inequality," he writes.

Viewed from either Emmott's or Waldron's point of departure — the necessity of preserving an open society or of respecting the moral equality of human beings — the surge toward widening inequality is endangering the West. As Emmott notes, without openness, the West cannot thrive. But without equality, the West cannot last.

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THE FATE OF THE WEST
The Battle to Save the World's Most Successful Political Idea
Bill Emmott
PublicAffairs
257 pages; $28

ONE ANOTHER'S EQUALS
The Basis of Human Equality
Jeremy Waldron
The Belknap Press/Harvard University Press
264 pages; $29.95