A mid-air misadventure

The more things change, the more they stay the same at AirAsia India

ANJULI BHARGAVA

So what if things continue in their usual dull manner at the Tata group's airline foray with Singapore airlines, Vistara? Slow and steady, hardly any staff changes and plenty of planned losses. There's never a dull moment at the group's second aviation venture in India — AirAsia India.

The latest is a series of resignations at senior levels at the airline. A few weeks ago the rumour mill had it that one of the top officials of the airline had been caught in a not-so-official position with a female co-worker while at work (a company spokesperson offered "no comment" when asked) and the incident had been reported to AirAsia Berhard founder Tony Fernandes, who chose to shoot the messenger, resulting in the resignation of the head of human resources at the carrier. In addition to the head of human resources, the airline also bid goodbye to its head of security, head of engineering and head of ancillary revenue and cargo, among a few others.

In June 2014 itself, when the airline took to the skies, it was off to a rocky start. In the first year, the airline managed to make quite a mess of its operations. To cite just one instance of how haphazard things were, AirAsia India is the only airline in India I can think of that managed to change hubs even before it took to the skies. It first announced Chennai but changed its hub to Bengaluru even before it launched — which, of course, was a better choice and an obvious one in the first place.

In the first year itself, many flights were introduced and withdrawn. Flight timing were, quite often, absurd. It announced ambitious expansion plans but failed to ramp up its fleet as envisaged. Losses totted up quickly and investors were forced to inject more equity earlier than anticipated. The airline had trouble retaining key people and most industry people I know treated it — and still do — as a sort of stop-gap arrangement while they looked for something more stable.

In August 2015, however, matters came to a head when certain financial irregularities were uncovered, leading to the resignation of its start-up CFO. The ripples of the financial troubles led to a full-fledged change in the team in March 2016, including a replacement of its rock star-like CEO who proved as poor as his words by yet another trusted aide of Fernandes, the second CEO to be put in charge with no experience in the airline sector. To everyone's surprise, Fernandes had a full new team on board (a CEO, CCO and CFO) with very little collective airline experience.

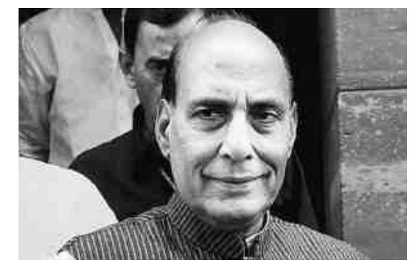
But here we are, over one year later, and very little seems to have changed at the airline. In addition to the latest spate of exits, the airline's operations seem as haphazard as before. With 12 aircraft and 1,540 employees (Vistara has just over 1,600 employees with 16 aircraft), it flies to 16 destinations. Instead of consolidating operations from one base, the airline has three hubs — Bengaluru, Delhi and now Kolkata. Instead of trying to increase frequencies on a particular route and thereby establish itself as a key player on that route, the airline is offering a host of single flights a day to various destinations. It plans to add a new aircraft next month and new flights on routes like Bhuvaneswar-Ranchi and Hyderabad-Ranchi, choices that appear quite random and bizarre to anyone who knows the Indian airspace.

If choice of routes is odd, so are timings. The airline offers a connection from Bangalore to Delhi at 11:50 pm, a flight that reaches Delhi at 2:30 am. There's a connection from Kolkata via Ranchi to Delhi at 4:45 a.m. The airline's losses continue to mount at a time when most rivals are making money for a change. A senior board member told me that the Tata's exposure to the airline was already causing them some alarm and he didn't think the group had a huge appetite left to invest further in the carrier.

This brings me to my final point on the whole AirAsia misadventure so far. As I see it, not only is it a huge wasted opportunity, it is one that is very difficult to comprehend. AirAsia India, in terms of timing, couldn't have asked for it to be better — the timing of its launch coincided with the fall of SpiceJet. The latter was tottering under the Maran stewardship and the space it vacated could easily have been filled by a new, more nimble rival.

But what is perhaps even more galling — and hard to comprehend — is the fact that AirAsia India had everything on a platter thanks to its parent. Be it manuals, systems, procedures, experience, training assistance or even uniforms, it only had to pick up the ball and run. Instead it stumbled.

CHINESE WHISPERS



Negative narrative

Home Minister Rajnath Singh said on Monday that anti-national elements have been trying to foment tension in the society by posting unverified information on social media and asked people not to forward such messages without verification. Singh, after launching the intelligence wing of the Sahastra Seema Bal (SSB), told the jawans that information and news, that was completely wrong or having no basis, was being regularly circulated on social media such as WhatsApp and many people consider it to to be true. Some days back, Bharatiya Janata Party chief Amit Shah had also cautioned supporters not to trust all that they read on the social media. The BJP has used social media, particularly WhatsApp, effectively in its election campaigns but there are indications of increasingly negative social media narrative against the Narendra Modi government in the wake of poor economic growth and steep petrol and diesel prices.

Tradition plus sensitivity

Bring back tradition but be sensitive to animals — that seems to be the mantra of Yaduveer Krishnadatta Chamaraja Wadiyar, the titular Maharaja of Mysuru, during this Dasara. The famous Dasara procession in Mysuru typically has a lead elephant carrying a howdah with a goddess idol. Wadiyar, who has a degree in English and Economics from Boston, has asked the government whether a set of elephants could pull a chariot instead of making the lead elephant carry the nearly 750 kg howdah for the 5.5 km stretch. The Karnataka government is yet to take a call.

Educating junior officers

Here's what a minister of state in the Narendra Modi government did when he realised that his subordinates were not keeping abreast of the happenings in his department. He decided to call status meetings. That would not be such a big deal if he didn't expect his team to get together at his office every day. Every team member is required to come prepared with up-to-date information on his or her area of operations, jot down notes on what's keeping the rest of the crew busy and offer suggestions and tips when a counterpart gets stuck.

Discounting the bullet train

Even the best estimates of future utilisation of such projects are often short of what really happens

SHREEKANT SAMBRANI

FRIENDLY GESTURE: Prime Minister Narendra Modi and his Japanese counterpart Shinzo Abe shake hands at the foundation stone-laying ceremony of the bullet train in Ahmedabad last Thursday. Modi has claimed Japan's contribution to the project is almost a free gift for India but experts have disagreed PHOTO: PTI

"It is kind of free," said Prime Minister Narendra Modi about the Mumbai-Ahmedabad High-Speed Rail project (referred hereafter by its popular name, the bullet train), in its ground-breaking ceremony last week. He was referring to its financing. Japan will provide ₹88,000 crore (81 per cent) of the ₹1.1 lakh crore cost as a 50-year loan at an annual interest of 0.1 per cent with a 15-year moratorium. These exceptionally favourable terms have led to a debate, as have several other features of this venture. Critics say that these parameters yield an unrealistic and overly optimistic internal rate of return for the bullet train.

Internal rate of return is one of the end results of discounted cash flow (DCF) analysis. This takes into account the time value of money for a multi-period project and is based on the reckoning of costs of opportunities forgone in choosing it.

A personal aside: The long-known DCF was introduced in the mid-1960s as part of the development economics curricula in universities. I was among the early students of this concept. I taught it in postgraduate courses and executive-training programmes. It was quite a novelty in the early 1970s and not very easy to get across. I have continued to use it extensively in my work.

Any undertaking providing benefits in the future involves sacrifice of some alternative use of the funds invested at present. The investment is justified if the sum of the stream of future benefits is greater than the value of present opportunities foregone. That sum needs to be discounted by an appropriate factor as it materialises not now but later, while the sacrifice is made at present. For investments with limited commercial objectives, such as those of private firms, the factor is the interest earned on own funds or paid for borrowed money. The discounting factor for projects with social benefits is based on weights the society attaches to present and future consumption. A very poor society with low consumption levels will use a high discount rate, while a rich one would use a fairly low one.

On this logic, the negligible rate of interest is the correct discounting factor for both India and Japan. There is little sacrifice involved in India, as Japan funds the project and since the loan is tied to it, investing the money on offer for other purposes is not possible. For Japan, the cost of funds is extremely low; in fact, not too long ago, Japan had a virtually negative bank rate. It would also create substantial additional demand for Japanese goods and technology in a new market segment.

The logic of using very low, near-zero, rates of discount for projects of long gestation and duration must prevail even when relatively poor societies invest their own meagre resources in creating facilities to provide desirable outcomes. Large irrigation and infrastructure projects are typical such instances. Leaving aside controversies on their distributional impact, these activities sometimes take a decade or longer before starting to generate sizeable benefits. Using prevailing interest rates as the discounting factor leads to a gross underestimation of the value the society would normally attach to these outcomes. Present values of benefits 20 and 25 years hence at a 10 per cent discount rate are 13 and 8 per cent of their nominal values respectively.

Conventional analysis is thus not quite relevant for investments which could be rightly termed as gifts that keep giving. We borrow money to own our housing even if the equated monthly installment of repayment is higher than the present rent for equivalent accommodation.

China made enormous investments in power plants, dams and world-class road and rail networks starting in the mid 1970s. The end result was its spectacular double-digit growth sustained over a long period and global economic dominance three and four decades later.

A relevant but much smaller Indian comparison is with the 1950s and 1960s decisions to establish Indian Institutes of Technology (IIT). Their feasibility could never have been established even without DCF given since they charged the students pittance as tuition. Yet one could assert without fear of contradiction that the alumni of these institutions created the image of excellence of Indian technocrats abroad, leading also to substantial homeward remittances earlier and now venture investments. Arguably, it was also the basis of the information technology revolution placing India in global limelight half a century later. Although neither of these were planned as results of IITs, they would not have happened in the absence of IITs (disclaimer: the writer is an early alumnus of IIT Bombay).

Questioning the Bullet train in view of the investment needed in Indian Railways is similar to saying that India needed to invest in primary education rather than in IITs. The fact is India in either instance needed both the activities. Much has been written recently, including in this paper, about the direct and indirect benefits of the Bullet train. We must also remember that this is a classic case of supply creating its own demand. Shekhar Gupta cites Konkan Railway and the Mumbai-Pune Expressway as examples of this ("Homeopathy as ideology," *Business Standard*, September 16, 2017). The short point is that even the best estimates of future utilisation of such projects are often short of what really happens.

Modi first visited Japan in 2006 as chief minister of Gujarat. He got five minutes with Shinzo Abe, who was the Japanese premier then too. That was a purely formal call, without any agenda. Modi also managed a ride in the Shinkansen train, including a visit to the driver's cabin. He told a bureaucrat accompanying him that he wanted to bring the bullet train to India. It has taken him a decade to do so. Luckily, he did not attempt to follow DCF analysis in this interim!

CONSUMER LIFE

Durables demand clutching at straws

MAHESH VYAS

Consumer sentiments shot up by an impressive 5.5 per cent during the week ended September 17. This is an unusually high increase of the consumer sentiments index during a week.

The pitrupaksh period did not dampen spirits in 2017, like it did not in 2016.

The proportion of households that said that this was a good time (compared to other times) to buy consumer durables increased to 26.2 per cent. This is higher than in any of the preceding four weeks. The past four weeks' average was 24 per cent. The proportion of households that said that this was a bad time (compared to other times) to buy consumer durables was 21.9 per cent which was a shade lower than the average 22.2 per cent proportion in the past four weeks.

On a net basis, 4.2 per cent households said that this is a good time to buy consumer durables. This is the highest ratio in the past four weeks.

If producers, retailers and marketing professionals of consumer durables have been led to believe that pitrupaksh is not the period to push sales, its time they revisited this theory. On the aggregate, the Indian consumer's decision to buy consumer durables does not seem to care much about pitrupaksh.

If there is a pitrupaksh effect then it is likely a self-fulfilling prophesy created by the supply chain. It is possible that stockists are more superstitious than consumers. It is also possible that if the supply chain tries hard to capitalise on auspicious days it is correspondingly compelled to accept the incrimination of inauspicious days.

India has progressed and maybe, it is time for consumer durables companies to see some change in their strategies.

Thanks to greater mobility of Indians, festivals are becoming a pan-India phenomenon. Mumbai will celebrate Navratri and Pujo beginning next week with as much fervor as it did Ganesh Chaturthi. Later, it will also celebrate Chhat Puja. Poor Biharis being beaten up in Mumbai was an unfortunate (and deplorable) short-term collateral damage of a relentless change that is underway. Festivals are not rooted much in tradition any more. They are the outcome of a search for celebrations, which can locate a sanction in our traditions and our culture.

Given that migration has engineered a pan-India celebration of all kinds of festivals, and given that consumers don't pay much attention to pitrupaksh, the consumer goods companies could do better to consider the entire period from Ganesh Chathurthi in August-September through Makar Sankranti or Akshay Tritiya in February-March to be a festive season, without interruption.

It is worth noting that both, rural and urban regions ignored pitrupaksh as consumer sentiments improved in both regions. The urban consumer sentiments index rose 2.8 per cent while the rural index rose by 6.7 per cent.

Yet, both have very different views with respect to buying of consumer durables, now. And the views are in stark contrast to their overall sentiment.

Rural folks displayed a robust, 6.7 per cent increase in household consumer sentiments during the week ended September 17. But, they showed no net improvement in their inclination to buy consumer durables. While the number of rural respondents who believed that this was a good time to buy consumer durables increased from 19.5 per cent to 21.4 per cent, the proportion of rural households that believed that this was a bad time increased from 21.1 per cent to 25.2 per cent. Rural India has been giving consumer durables a thumbs-down similarly since early August.

However, most of the demand for consumer durables is in urban India. And here the story is somewhat promising, but only a bit.

During the week ended September 17, 28.6 per cent of urban households said that this was a good time to buy consumer durables. This is a recovery from a persistent fall since late July; and it is closer to the average.

The proportion of respondents who said that this is a bad time to buy consumer durables dropped quite sharply from 23 per cent to 20.3 per cent. Yet, it was high compared to the average of 18 per cent.

While the proportion of urban households who think it is a good time to buy durables has been steady, the proportion who believe it is a bad time has been increasing.

The BSE-CMIE-UMich consumer sentiments indices seem to suggest that the demand for consumer durables in the coming festivals season is not at its best but, it did improve in the last couple of weeks, even if just a wee bit.

The writer is managing director and CEO, Centre for Monitoring Indian Economy

LETTERS

Consider social impact

Apropos "PM inaugurates Sardar Saravor Dam; calls it engineering marvel" (September 18), the controversial project on the Narmada, the largest and most expensive such project in the country, is considered by many environmentalists, academics, economists and activists as the largest planned ecological disaster. Though its proponents claimed it as the most studied river valley project , comprehensive environmental impact assessment had not reportedly been done. Besides, major conditionality set down by the Ministry of Environment and Forests have allegedly been unheeded.

The prime minister in his address mainly targeted academics, activists, and the World Bank. From the very inception of the dam, a large number of environmentalists, economists, communists and intellectual of international repute such as Noam Chomsky protested, apprehending the possible devastation of environment and loss of livelihood of millions of people. Though the World Bank had originally supported the SSP with a $450-million loan, it withdrew it as the environmental and social impacts of the project had not been properly considered. By referring to the monetary support extended by the temples in Gujarat, the PM has perhaps tried to satisfy the Hindutva organisations just before the Assembly elections in the state.

Needless to say, the environmentalists all over the world mull that big dams not only upset environment and its ecosystem but also produce huge amount of green house gases expediting the process of global warming. When a large number of dams have been demolished the US to save the rivers and environment as well, our country with utter lack of pragmatism, takes pride in building the world's second largest dam on the river Narmada.

Buddhadev Nandi Bankura

Robbing Peter to pay Paul

With reference to the news report "Don't exploit the country, keep price below ₹40k a tonne: Govt to steel firms" (September 17), the government has recently taken steps to ringfence the steel industry from the onslaught of cheaper imports as it is of the considered view that India can't be used as a dumping ground and a balance has thus to be constantly maintained. How come then that the BJP-led NDA govt has constantly been "exploiting" the hapless common man by hiking the petrol prices across the country?

Ministers are publicly justifying the same even when engaged in the act of robbing Peter to pay Paul. However, the government should not underestimate the power of the common man. Mind you, nothing is permanent here which obviously includes the people mandated political power centres.

Kumar Gupt Panchkula

Avoidable issues

During the past three years, there have been several reforms in the taxation system in India. The goods and services tax (GST) has been claimed as a revolutionary step in the direction of improving and simplifying taxation and tax collection procedures. Initial hiccups are many. Some of these should have been avoided to ensure that whatever credibility in the public mind remains of the government's intentions is not further eroded.

It's well known that there was tax evasion before the GST days and therefore collecting the GST would be unavoidable in certain situations. But this needs to be done transparently. Many sales and services outlets are straightaway adding another 18 per cent GST to the pre-GST price which give rise to genuine apprehensions in the minds of customers. Perhaps, central and state governments could nominate district level ombudsmen to receive customers'/consumers' grievances in such situations.

M G Warrier Mumbai

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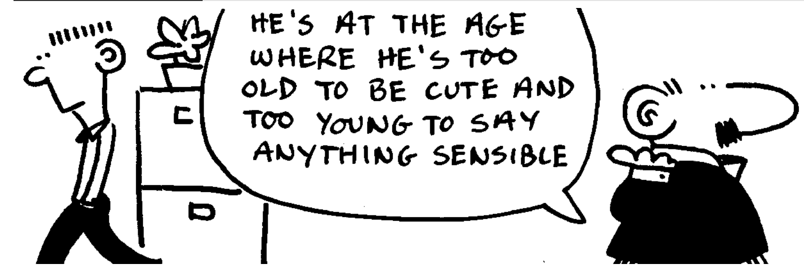
HAMBONE BY MIKE FLANAGAN



Business Standard
Volume XXII Number 26
MUMBAI | TUESDAY, 19 SEPTEMBER 2017

Cracking the shells

But the principle of natural justice should not be ignored

The government has intensified its crackdown on shell companies — while some 210,000 companies have been deregistered and their bank accounts frozen, pending further investigations, over 100,000 individuals who held directorships in these organisations have been disqualified. Professionals such as company secretaries and chartered accountants suspected of having enabled tax evasion have been placed under watch. The authorities have also threatened to apply penal provisions to any person who has attempted to siphon money from accounts of shell companies. This follows close on the heels of the decision by the capital markets regulator, the Securities and Exchange Board of India, to freeze trading in many listed companies on the ground that these entities were used for the purposes of money laundering and tax evasion.

The intention behind these concerted actions is laudable. The decision to turn attention towards shell companies cannot be faulted, for it is widely known that lax regulations allowed many errant promoters to list companies with no operations and these were used as a conduit for money laundering. Plugging such loopholes in the corporate system should eventually result in a cleaner financial environment where there are fewer cases of tax dodging and other illegal activities.

However, the government should guard against taking unilateral actions against corporate entities and individuals on mere suspicion of such acts as this could end up hurting the innocent. This is particularly important to erase the perception that provisions such as Section 164 of the Companies Act, 2013, pertaining to disqualification of directors, can be applied selectively to harass political opponents of the current dispensation. Second, and this is more serious, the innocent may suffer in the case of precipitate actions and blanket bans. For example, Sebi had banned trading in the shares of many companies without giving the entities in question a chance to respond to the allegations. In fact, that incident proved embarrassing. The Sebi action set off a mini-crash in the market, affecting the prices of multiple shares and leading to the destruction of wealth of many financial institutions and individual investors. Sebi subsequently rescinded the trading ban on many of those companies, tacitly admitting that the charges against them held no water. But the damage to corporate reputations and to the net worth of investors was considerable.

Similarly, there could be some individuals amidst that vast list of debarred directors who had nothing to do with the activities of these firms and, indeed, there may be firms that are subsequently exonerated of the charges laid against them. Such persons or entities will suffer an unnecessary loss of reputation. The government should definitely proceed against companies where there is credible evidence that attempts have been made to launder money and dodge taxes, but given that such organisations and individuals are already on the watch-list, the authorities should ensure that while banning institutions and individuals, the fundamental principle of natural justice is not given the short shrift. That is a prerequisite for a healthy corporate environment. The other problem is that the Companies Act has not defined what a "shell company" is and what kind of activities would lead to a company being termed a "shell". This gives rise to a lot of loose interpretations about the definition of a shell company. This also needs to be rectified through suitable amendments in the law.

High-speed success

The bullet train project needs to buck many trends

At a cost of ₹1.1 lakh crore and an ambitious completion date of five years, the Mumbai-Ahmedabad bullet train, inaugurated with much fanfare by Japanese Prime Minister Shinzo Abe last Thursday, will be India's most challenging transport-related public project to date. The technology complexity is one dimension of the issue – India still does not have a train that can be classified as high speed by international standards. India's well-established patchy record on project implementation also presents justifiable cause for doubt. The bullet train will run at speeds of over 300 kmph, which is no small leap of faith when the Indian Railways is still struggling to introduce semi-high speed trains – those that run at a top speed of 160 kmph – and our "express" trains run at an average speed of 50 kmph. Taken together with valid misgivings, such as the risky financing model, subject as it is to the rupee-yen exchange rate, and the conventional railway's grimly deteriorating safety record, the bullet train project will have to buck many trends to fulfill Prime Minister Narendra Modi's ambitions of reflecting a "new India".

There is no silver bullet here, so to speak, and the ability to absorb sophisticated technology will be the least of the problems, as the Konkan Railway project or indigenously designed missiles and space missions have proven. But to seamlessly implement a project of immense complexity, laying 508 km of sophisticated high-speed tracks partly on elevated corridors and partly under the sea and acquiring some 825 hectares of land that will displace over 2,700 families, requires more than just scientific and engineering prowess. As a starting point, it will mean establishing an institutional structure that can be empowered to function outside the traditional *sarkari* apparatus and maximise efficiency. Luckily, the government has a handy model in the Delhi Metro Rail Corporation (DMRC), also partly bankrolled by Japanese institutional finance and technology partnership, on which to predicate the bullet train project. Notwithstanding some glitches, such as the failure of the private-public participation venture for the airport link and some faulty construction, the Delhi Metro has attracted widespread approbation not just for timely completion but for achieving the "hygiene" factors – safety, cleanliness and punctuality – that Western or south-east Asian cities take for granted. In a country famed for its rundown urban transport systems, the very visible world-class quality of the Delhi Metro has encouraged several other cities to opt for similar models.

DMRC, thus, has become a consultant in its own right, now advising metro projects both in India and abroad (Jakarta and Dhaka being two of them). One critical and often overlooked reason for DMRC's success is that E Sreedharan, Delhi Metro's moving force, stipulated that he be given a free hand and shielded from political interference as preconditions for meeting project targets. It is fair to say that the political dispensation largely honoured those terms. If New Delhi is able to empower the executors of the bullet train project in a similar manner, it, too, could become a showcase project for India and prove the doubters wrong.

ILLUSTRATION BY AJAY MOHANTY

Is 3G the future of consumer firms?

With increased volatility, managements best suited to create moats around businesses might lose out to frequent changes

The firm 3G Capital, a private equity shop, and its principals have an enviable track record in creating shareholder value across consumer businesses. They have been instrumental in creating and operating ABI (Anheuser-Busch InBev), the world's largest brewer with 28 per cent global market share, Burger King (now Restaurant Brands International), and Kraft Heinz (KHC).

Across the three companies they have created significant shareholder value. This has come largely through margin expansion. In the case of ABI, US earnings before interest and taxes (EBIT) margins went from 23 per cent to 36 per cent. For Burger King earnings before interest, taxes, depreciation and amortisation (Ebitda) margins rocketed from 18 per cent to 69 per cent (went entirely franchised) and in the case of KHC, Ebitda margins have improved from 18 per cent to 30 per cent. These margin gains have been both organic and driven by cost takeout after acquisitions. In the typical 3G capital deal, they have managed to take out 16 per cent of the target company sales as synergy benefits.

AKASH PRAKASH

How does 3G capital do this margin expansion? First of all, they aim to create a culture of ownership. Their transformation of companies is as much cultural as financial engineering. They come into companies with entrenched ways of doing things and bring in their own people, put in their own operating philosophy, and incentive structures. The ownership culture means employees are encouraged to think long term and be accountable. Compensation is skewed to variable pay and stock incentives are aligned with a minimum holding period of five years. Creating this ownership culture is the biggest piece of the secret sauce. They aim to minimise the agent-principal problem.

They are also very focused on inculcating best practices from both within their portfolio companies and across industries.

They scrutinise in exquisite detail all expenses dubbed as non-working money — money spent not directly growing the business. Everything in this bucket has to be justified on zero-based budgeting principles, with ownership of every cost line. This is where the bulk of the cost cuts occur.

The other bucket of costs, dubbed as working money, any expense used to directly grow the business, is actually supported and in many cases increased. In this bucket we have advertising and new plants for example.

Then we have other people's money, basically leverage, which is used to boost equity returns and fund acquisitions and make it a virtuous circle.

3G Capital, through its acquisition of Heinz and then Kraft, has now targeted the consumer packaged food (CPG) space for disruption and value creation. The failed acquisition of Unilever, however, indicates that they will not stop at food; the entire consumer space is in their crosshairs.

When looking at KHC, 3G Capital saw a very complacent and inbred culture affecting the entire packaged food industry. These companies were used to limited change and disruption as the barriers to entry for a new player were very high. They were able to deliver years of double-digit shareholder returns with only 1 per cent volume growth (in line with population growth). These companies had no need to focus on their cost base and complacency led them to become complicated, inward looking and flabby organisations. All the major companies were run by long-term industry veterans and insiders, with almost no senior talent coming from outside.

The stable annual double-digit shareholder returns delivered across the consumer space are now under question, as the barriers to entry of limited retail shelf space, need for national TV, and slotting fees are falling by the wayside. Consumer stocks are having to fight fragmentation, distrust of large brands and millennials' focus on health and wellness. The new shareholder return mantra seems to be negative volumes and zero returns at best. In such a scenario there seems little else that consumer companies can do except follow the 3G Capital template of cutting costs, raising margins and using leverage to boost returns and consolidate the industry. Cost cuts are the only way to overcome the headwinds of declining volumes. However 3G Capital was able to implement these cost cuts by bringing in new management and an ownership mindset. The average age of the KHC leadership is only 43 years compared to 53 years for its peers. About 70 per cent of the KHC leadership has come from outside the food industry, compared to sub-20 per cent for its peers. These figures highlight the difficulty other consumer stocks will have in implementing the 3G Capital game plan. The 3G Capital template requires gut wrenching changes in culture and significant social costs. Management teams which have grown up in the security and stability of high barrier to entry consumer businesses, may not have the experience or skill sets to execute cost cuts, manage leverage and implement genuine zero based budgeting, all needed to drive shareholder value in the new paradigm of consumer disruption.

If the existing management teams cannot deliver, expect activists or companies like KHC (through acquisitions) to force the changes needed.

Disruption has arrived in the consumer space. Understanding your company's management team and its adaptability to handle a fast-changing consumer environment may be the single biggest determinant of stock success in the coming years across the consumer space. The very stability of revenues and margins of the past create the difficulty in adjusting to the new normal of vastly greater competition and limited barriers to entry. As disruption spreads, many of the champions of yesteryear will fall by the wayside. Variability of single stock returns will increase dramatically. The better the business and the stronger it's moats the more difficulty it will have in adjusting to disruption. The management teams best suited to strengthening the moats around the business may be the most ill-suited to drive organisational changes needed to grow and survive in the new paradigm of increased volatility.

The writer is with Amansa Capital

Rajan in the limelight again

Former Reserve Bank of India (RBI) governor Raghuram Rajan came, he saw, he conquered the media. For a year following his exit as RBI governor, Dr Rajan had chosen to maintain silence on the Indian economy. During his recent visit to India, it was hard to open a newspaper or switch on a channel without seeing an interview with him.

The interviews covered pretty much the same ground, with the focus always on demonetisation. Dr Rajan said many things that would have gladdened the hearts of those critical of the initiative. Yes, he had expressed his reservations when the proposal was put to him. And, yes, he thought the short-term costs were steep — he mentioned estimates in the range of 1-2 per cent of the gross domestic product (GDP). And, yes again, he wasn't sure the long-term benefits justified the costs. It's fair to say that Dr Rajan hasn't added anything to the debate on the subject. We do not have a handle yet on either the costs or the benefits of demonetisation.

FINGER ON THE PULSE

TT RAM MOHAN

The focus on demonetisation was a bit unfortunate as it overshadowed some pretty strong remarks Dr Rajan made about the banking system. Dr Rajan expressed reservations about mergers of public sector banks (PSBs). He warned that it would be unwise to attempt mergers at a time when PSBs were weak and wrestling with the problem of high levels of non-performing assets. One hopes the finance ministry is listening.

Dr Rajan was equally forthright on the need to do what it takes to recapitalise PSBs. He went so far as to say that the government should provide the necessary capital to PSBs even if it meant cutting allocations on other heads. The government and the top brass at the RBI have been telling us that some PSBs are so hopelessly deficient in managerial capabilities that putting more capital into them is money down the drain. Rajan clearly doesn't think so.

We have thus far got banks to clean up their balance sheets without providing them the necessary capital. By many estimates, PSBs would require another ₹1 lakh crore in order to meet the regulatory capital requirement. The Budget for this year has provided for just ₹20,000 crore. Dr Rajan believes this is a sure recipe for holding up growth in credit and private investment.

Dr Rajan's views on reform of governance at PSBs are rather more debatable. He wants the Banks Board Bureau (BBB) to have greater autonomy from the government. He would like the Department of Financial Services (DFS), whose job is to monitor PSBs, to be closed down. He wants PSBs to be monitored entirely by independent boards, presumably appointed by a truly independent BBB.

These views have wide currency today. However, the notion that PSBs should be freed from the supposed tyranny of the DFS is conceptually flawed. It overlooks a crucial fact about the governance model that obtains in India: Ownership of enterprises, whether in the public sector or the private sector, is not widely dispersed, as it is in the Anglo-Saxon model. We have instead a dominant owner in either the government or in industrial houses.

Where there is a dominant owner, the role of the board is rather more limited than in cases where ownership is widely dispersed. It is natural for the dominant owner to call the shots. The government cannot be expected to adopt a hands-off policy towards PSBs any more than Tata, Birla or Ambani can in their enterprises.

Moreover, it is possible to overstate the effectiveness of "independent" boards. Boards the world over are notoriously ineffective, which is why corporate governance is still work in progress more than two decades after the movement began. Those familiar with the working of PSBs would know that it is the government director and the RBI director who often make the most meaningful interventions.

Leaving matters at PSBs entirely to independent directors could, therefore, create a dangerous governance vacuum. There remains a case for the DFS to play a monitoring role. What is undesirable is that the DFS should issue directives to the CEOs of PSBs. Instead, the DFS should communicate its views through its nominee directors on boards, thereby strengthening the effectiveness of boards.

What Dr Rajan did not say is also significant. Dr Rajan is no foe of the private sector. Yet he made no mention of privatising any of the PSBs. Dr Rajan's silence on privatisation at a time when "strategic sale" is the buzzword should make the finance ministry sit up and take note.

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Bimal Jalan reflects

BOOK REVIEW

SANJEEV AHLUWALIA

Bimal Jalan exercises the writer's privilege to box his reflections between three inflection points. The first is 1980, ostensibly because 1977-79 was the first time the Congress lost power at the Centre. The second is 2000, being the start of a new millennium. And 2014 is the bookend when the Bharatiya Janata Party (BJP)-led National Democratic Alliance (NDA) formed a majority government.

Of these, the choice of the first two years as turning points is not immediately obvious. Conventional wisdom regards 1991 to 2014 as a near continuous development period, barring the fractious interregnum of 1997-99. In the 1980s, it is 1984 that dominates, as the end of an era with the assassination of Indira Gandhi and the beginnings of Rajiv Gandhi's brief "Camelot" phase. The year 1980 is significant only because Sanjay Gandhi died in an air crash in June and Mrs Gandhi aged visibly. The choice of 2000 is similarly obscure, except for broadly coinciding with the start of Atal Bihari Vajpayee's NDA government.

But this is mere quibbling. The book is unconstrained by structural rigidities. It provides reflections, spanning Dr Jalan's seven earlier publications since 1992. It can't get better. Dr Jalan was in the Rajya Sabha (2003-2009); governor of the Reserve Bank of India (1997-2003); finance secretary; secretary banking, chief economic advisor and India's executive director to the IMF and the World Bank.

Readers would choose their own favourite reflections. But this reviewer was intrigued by the following seven. First, Dr Jalan favours the conventional view that the persistent gap between India and the fast-growing economies of Asia during the last four decades of the 20th century is explained by our low levels of investment. He squarely blames our ideological decision to invest in public sector industries, which failed to generate savings for future investment and instead bled scarce tax revenue to fund financial losses — a familiar story even today.

Second, he red flags the fact that from the 1970s, we did very little to enhance the competence and efficiency of public administration. We still lack the required composition of skills and experience in the public space to provide 21st century results.

Third, he bemoans the fact that we unfailingly adopt best practice priorities — take the national priority for agricultural growth. But we fail miserably in making supportive policies and rules. We have throttled agriculture by ignoring the interest of the farmer to serve the interest of the consumer. Similarly, we prioritise a progressive fiscal policy. But the revenue from direct taxes stagnates while regressive indirect taxes are buoyant.

Fourth, Dr Jalan's term in the Rajya Sabha convinced him that deep political reform is the key to change India. And who could disagree? But some caveats apply. Decentralisation, as flagged by Jalan, is certainly desirable for enhanced effectiveness and public participation. But, it will not, by itself, serve to reduce the size of government. In fact, employee numbers and expenses are likely to increase as scale effects disappear.

In a similar vein, it is true that the Union government tends to erode the federal structure by misusing governors for narrow political ends. But constitutionally, we are a "Union of States with a centrist bias", per political pundits, and not a federal state. Parliamentary norms and conventions are routinely subverted — a self-goal, since this reduces Parliament's credibility.

Dr Jalan cites 2006, when the budget was passed without discussion, illustrating political expediency of the worst kind. But it is open to question whether the existing process for annual Budget presentation and examination remains a productive exercise or has become mere form without substance. The cabinet system of decision-making, underpinned by the principle of collective responsibility, was undeniably subverted during the United Progressive Alliance government, since political power was dispersed beyond the government. But this was poor practice rather than a structural flaw. And it appears to have healed itself after 2014.

Fifth, the judiciary, rightly, comes in for high praise, for progressive jurisprudence, safeguarding the principle of separation of powers, and the primacy of the Constitution. But entrenched territoriality in the judicial appointments process remains contentious.

Sixth, Dr Jalan recounts, financial reforms after the Narasimham Committee report of 1998 enhanced the resilience of Indian banks. But he leaves the reader begging for more on what went wrong over the last decade to inflate stressed loans to crippling levels. Are not politicised leadership and boards the problem in public banks? And given the stakes, can UPSC selection – as Dr Jalan suggests – really be an effective bulwark? Would not ramping up private shareholding, with the government holding only a "golden share" be a more effective solution? More generally, how effective are the existing prudential norms, for limiting exposure to sector, corporate or currency risk?

Seventh, Dr Jalan's view that it is unnecessary to reopen the constitutional scheme for inter-governmental division of taxes is curious. Tax pundits advocate that GST be extended to alcohol and petroleum.

It is a broad canvas on which Bimal Jalan reflects, as befits one who has helmed public policy since the 1980s. Readers will look forward to his take on the more recent developments — that is, since 2014.

INDIA
Priorities for the Future
Bimal Jalan
Penguin-Viking
256 pages; ₹499