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# Opinion

FRIDAY, SEPTEMBER 15, 2017

**BULLET VIEW**

Japanese prime minister Shinzo Abe

"I hope that in a few years when I come to Ahmedabad, I ride the Shinkansen train with Modi while chatting with him and viewing beautiful sights from the train's window"

## RationalExpectations

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# Is Piketty right, and what do we do?

Apart from his model being iffy, inequality is function of growth – more jobs will help, but not clear by how much

**EVEN A CASUAL** observer can tell you inequality levels have gone up in India over the past few decades, so when a new paper by Thomas Piketty and Lucas Chancel present a series of data to show this, it is hardly surprising. Between 1951 and 1980, the duo say, per capita incomes for the bottom half of the population grew by 2.2% per annum but when overall income growth for the country almost doubled—from 1.7% to 3.3%—in 1980-2014, the bottom half's incomes grew by a lower 1.9%. For the middle 40%, income growth rose, but not by much—from 1.9% to a bit over 2%. For the top 1%, in contrast, income growth rose from 0.2% to 6.7%. It is when you look at that over a longer period of time that the differences really hit you (see table). So, the bottom 50% saw income growth rise marginally from 87% to 89% over the two periods while the top 1% saw income growth rise from 5% to a whopping 750%.

How accurate is the Piketty data, is the obvious question since the higher growth period is also the one that saw a massive fall in Indian poverty levels, and certainly the consumerism of the last few decades can't be reconciled with the Piketty/Chancel view that 'shining India' was restricted to just the top 10% of the population.

Before examining how good Piketty's data is, even this suggests rising inequality appears to go hand in hand with higher growth. The country that has the most equal growth, France, is also the one with the slowest growth. China has more inequality than the US, but its growth is also much faster—India's inequality is higher than that of China but less than that of the US. It may be true, as James Crabtree says in his piece on Piketty, that nations with great inequality tend to grow more slowly, but that's probably true after a certain level of income. It is difficult to name any country that has risen from the kind of abject poverty that China and India have without rising levels of inequality.

Though several vital flaws were pointed out in Piketty's *Capital in the Twenty First Century*, not too much work has been done as yet by economists/statisticians on the Piketty/Chancel paper. Even so, several assumptions look worrying. Since India does not collect data on incomes but only on expenditure, Piketty/Chancel blithely marry consumption data from the National Sample Survey (NSS) and the income tax since, in their words, "our preferred strategy is to assume that surveys are reliable from the bottom of the distribution up to a certain percentile and that tax data is reliable after another"! Even if you assume the tax data does represent those in the upper strata, there is enough reason to believe the NSS is mostly junk, even for those in the lower segments. Between 1983 and 2011, as the duo acknowledge, while GDP data show household consumption expenditure grew by over 300%, the NSS indicates it grew just 200%—so incomes at the bottom are vastly understated. Other data in the paper, that feed into the same narrative of the rich exclusively cornering all the benefits of growth, look equally odd—a *Forbes' India* Rich list shows the wealth of the richest Indians at less than 2% of GDP in the 1990s, rising to a peak of 27% in FY09 and then collapsing to 10% in 2015; there is nothing, however, to explain why it collapsed since asset prices have risen steadily in this period.

But let's forget all of this and assume Piketty is right. What is the policy prescription this suggests that is different from what various governments have been attempting to follow? Better education and health are obvious ways to increase the lot of the poor, but funding that requires a quantum leap in tax collections—that's exactly what every government since 1991 has been attempting to do. The same holds for improving infrastructure and easing various doing-business rules which will help create both more jobs as well as entrepreneurs. But since the knowledge economy will create even more inequalities—just see Apple/Google's meteoric rise to know this—a policy most favour is to rapidly increase taxes on the rich. When money moves so quickly to low-tax jurisdictions, though attractive, this is perhaps the most destructive policy to follow; indeed, it will take India back to the 'glorious' days of Indira Gandhi—high on rhetoric and poor on delivery.

**Rich benefit more in high-growth phases**

Cumulative real growth in per adult incomes (%), by percentile

| | INDIA | | CHINA | USA | FRANCE |
|---|---|---|---|---|---|
| | 1951-80 | 1980-2014 | 1980-2014 | 1980-2014 | 1980-2014 |
| Full population | 65 | 187 | 659 | 62 | 35 |
| Bottom 50% | 87 | 89 | 312 | 4 | 25 |
| Middle 40% | 74 | 93 | 615 | 45 | 32 |
| Top 10% | 42 | 394 | 1,074 | 119 | 47 |
| Top 1% | 5 | 750 | 1,534 | 198 | 88 |

## FuellingGROWTH

Had govt not mopped up taxes from oil sector, its capex and spending—vital for GDP growth—couldn't have risen

**THAT THE OPPOSITION** should portray the government as a tax-grabbing one, preventing consumers from benefitting from the collapse in global crude oil prices—from $105 per barrel in FY14 to around $50 today—is par for the course. Between central government excise duties and state VATs, taxes in Delhi comprise around 52% of the retail price of petrol and around 44% in the case of diesel. VAT rates, in fact, vary dramatically across states, from 27% in Delhi to as much as 48% in Maharashtra (on petrol). As a result, petrol in neighbouring Pakistan is cheaper by ₹28 per litre and by ₹20 in Sri Lanka. As the 2016-17 Economic Survey points out, the Centre has pushed up the excise duty on petrol by almost 150% since July 2014. As a result, central revenues from the sector rose a whopping ₹86,377 crore in FY15 and ₹76,091 crore in FY16—the bulk of this was from taxes. While states didn't see much of an increase in VAT rates in FY16, they realised the potential and raised revenues by ₹29,561 crore in FY17.

At a time when most growth-drivers of the economy—consumption, investments and exports—are either slowing or contracting, it was critical the government step up spending in a big way. At the same time, keeping control on the fiscal deficit was important, else the signal to bond markets would raise interest costs and negate a part of the increased government-capex. It is the higher taxes on petroleum that everyone seems to be up in arms against that helped the government—both the Centre and the states—sharply step up both capex and other expenditure while keeping the fiscal deficit under control. Between FY15 and FY17, total petroleum sector revenues for both the Centre and the states rose from 2.7% of GDP to 3.5%. As a result, the contribution of government expenditure to GDP growth has shot up; in terms of the multiplier impact of roads and railway construction, for example, it is far greater.

**FAKE NEWS**

IF PEOPLE CAN ENGAGE THEIR CURIOSITY, IT DOESN'T MATTER WHO IS SMARTER

# Ignorance feeds curiosity. Curiosity cures ignorance

FAYE FLAM
Bloomberg

**SCIENTISTS HAVE STEPPED** up their investigations into fake news in recent months, and amid all the analyses, studies and meetings, some have raised the possibility that a lot of people simply don't care whether the claims they embrace are true. "Post-truth" has become a hot topic for researchers from a variety of fields, including Nobel prize-winning chemists: The annual Lindau Nobel Laureate Meeting in Germany this summer took as a theme *"Science in a Post-Truth Era"*.

Sceptics have long studied why people wrongly believe in astrology, ESP and all manner of weird things, but not caring about truth at all would seem to fly in the face of basic human curiosity. People send probes to other planets, dig up dinosaur bones, and build powerful microscopes to find out the truth about inner and outer space. We follow crime stories because we want to learn what really happened. Shouldn't curiosity act as a guardrail to keep us from falling into a post-truth world?

Astrophysicist Mario Livio makes a key observation in his new book, *Why?: What Makes Us Curious*: To be truly curious requires a middling level of knowledge. If you know absolutely nothing, then you don't know what to be curious about. If you know everything, you have no reason to inquire. So children who have never heard of dinosaurs can't be curious about them, and very few adults are curious about how many pennies are in a dollar.

I realised, however, that it's not actual knowledge but people's perception of their own knowledge that encourages or stifles curiosity. That observation snapped into place for me at an event at the MIT Media Lab. In a talk, Putin biographer Masha Gessen noted that one striking similarity between Russian president Vladimir Putin and US president Donald Trump is their utter lack of curiosity. I asked her to elaborate, and she said that both men think they already know everything. That perception of superior knowledge comes through in Trump's habit of saying "Nobody knows it better than me" when discussing a variety of subjects—taxes, trade, visas, infrastructure, social media, uranium sales, and "nuclear horror," to name a few.

So, curiosity requires a level of humility. But how far does the problem of ego inflation go? In his new book *The Death of Expertise*, author Tom Nichols makes a case that there's a raging epidemic of egomania in the United States. "Most cases of ignorance can be overcome if people are willing to learn," he writes. "Nothing, however, can overcome the toxic confluence of arrogance, narcissism and cynicism that Americans now wear like full suit of armour against the efforts of experts and professionals."

Nichols is not convinced that curiosity matters to the bulk of the public. Sure, he said, some people are curious—the engineers and scientists and artists of the world. But he doesn't see curiosity as an important driver of human behavior. "People don't go on Reddit to learn stuff—they go there to win," he said. If they read newspaper or magazine stories at all, he argues, it is not to satisfy a thirst for knowledge, but to look smart or to collect likes on Facebook.

Of course, not everyone takes such a dim view of human curiosity. In another book about expertise, *If I Understood You, Would I Have This Look on My Face?*, the actor and science advocate Alan Alda takes for granted that many people are hungry for knowledge. But to engage that curiosity, he argues, experts have to pay attention to their audiences to gauge where they fall on that spectrum of intermediate knowledge. By listening and communicating, experts can avoid talking over people's heads or repeating things they already know—both mistakes scientists sometimes make.

> To engage curiosity, experts must pay attention to their audiences to gauge where they fall on the spectrum of intermediate knowledge. By listening and communicating, experts can avoid talking over people's heads or repeating things they already know

Alda is himself a curious character. He became involved in science communication after hosting the television show Scientific American Frontiers. He realised that scientists often find themselves onstage or in front of cameras struggling to explain their research, and thought his expertise in acting and improvisation might prove useful. Now he's adapting his ideas for business leaders and other experts.

One lesson from improvisation, he says, is that real communication is an exchange, and what you say should depend on what you see and hear from the other party. When I spoke with Alda, he made the memorable observation that everyone knows things you don't know—whether you're speaking to an astrophysicist or the person who cuts your hair or delivers your pizza. They have different experiences. They have seen the world from different angles. If people can engage their curiosity, it doesn't matter who is smarter. What matters is that both parties leave the encounter smarter than they were before.

William Moerner, a Nobel Laureate in chemistry, is one of those curious people. I was interviewing him about various topics after he had spoken at the meeting of Nobel winners in Germany, when the US's decision to cancel a national commission on forensic science came up. He wanted to know what I knew. He had a notebook and pen in hand, and by the end of our chat, he may have asked as many questions and jotted as many notes as I had.

While he had been onstage during the panel discussion, another journalist asked him why he wasn't more outraged, given the way the US government was sidelining science. Indeed, the world (and especially the world of social media) seems to demand indignation. But outrage hinges on certainty—not on that intermediate level of knowledge that stimulates investigation and curiosity. Moerner's response? At times like this, he said, "Someone needs to be rational."

# Easing investment in commodities

Commodity index investing through ETFs is the most popular way of getting exposure to this asset class

V SHUNMUGAM
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Views are personal

**INVESTORS SOMETIMES** have the apprehension that investing in commodities is complex and risky. An investor might think that such investing requires owning the commodity and having access to storage. This is not necessarily true. Financial instruments, including commodity derivatives, offer investors a chance to invest in this asset class without having to worry about physical delivery of the commodity, which can indeed often be unnecessary and costly. However, trading in commodity derivatives encounter the obstacle of contracts' expiry: derivative contracts come with an expiry date and for the investor to have continued exposure to the commodity, they must re-invest or 'rollover' the contracts nearing expiry to contracts that are further from expiration.

Indices offer investors an easy avenue to invest in the market of commodity derivatives. The ease of this route lies in that investors have to base their investment decisions only on the expected movements of the index, without having to worry about other paraphernalia associated with commodity derivatives trade. Thus, investors can benefit from the performance of the index without having to deal with roll-over or handling delivery on expiry of the derivatives contracts traded on an exchange. Additionally, commodities in a broad or composite index are often not highly co-related to each other and therefore the index returns are less volatile than the returns on individual commodities. Thus, commodity index provides an investment tool which not only offers effective diversification to a portfolio but also offers an array of risk-return profiles for investors to choose from. This fits quite well in the psyche and investment preferences of the average Indian investor.

So, what are commodity indices? Commodity indices are those that track the prices of different constituent commodities and measure their performance. The components of a commodity index can vary from energy to precious metals, base metals, agriculture or their combination with pre-assigned weights. The performance of the index is tracked through the prices of its constituent commodity contracts and the value of the index linked to the prices of the underlying commodities.

Nevertheless, all commodity indices are not alike. Commodity indices may be broad based including important and liquid commodities from different sectors in a basket, or they may be sector-specific or even single commodity-specific. Even if the composition of two indices are same, differences in the weights of their components may make one more representative, or more profitable for investment, than the other. An investor can invest in commodity indices both directly and indirectly. They can directly trade derivative contracts with a commodity index as the underlying; or they can invest by trading in units of an index-based ETF. Globally, index linked products are also made available by the financial institutions as over-the-counter (OTC) products for the investors matching their risk and return profile.

Commodity index investing through ETFs is the most popular way of getting exposure to this asset class in most jurisdictions where this is allowed. Apart from providing a hassle-free and simple way of investing in commodities, they are offered and managed by institutions which are mostly under the radar of regulatory bodies, which adds to their appeal for retail investors. This makes commodity index-based ETFs popular all across the world. As of July 2017, the total outstanding commodity assets of ETFs globally amounted to $190 billion. Most of these ETFs aim to outperform or replicate a benchmark index.

In developed markets, fund houses employ various strategies in managing commodity-based ETFs, a few of which are mentioned in the accompanying graphic.

The role of commodities as an asset class is widely recognised due to its unique characteristics as a protector against inflation and safe haven nature. With negative correlation to most other financial asset classes, inclusion of commodities in any portfolio enhances the risk adjusted returns and thereby offering a better value to the investors. Commodity indices provide a simple approach to getting exposure to this asset class, which, if accessed with financial instruments which are well-regulated and transparent, can provide retail investors with sound and safe returns. With category III AIFs being allowed by regulators for participation in the commodities derivative markets, they can construct a portfolio in an effort to benchmark the composite index. To the investors in such funds, the movement of the index provides a clear picture of the net asset value of their investments, thereby providing them the with necessary comfort and convenience. Derivatives on commodity indices could also be traded when allowed to provide a risk return profile matching the aggregate movement all underling commodities in the given basket of composite indices; however, tradable commodity indices are not yet available, and when permitted, would provide yet another opportunity for participants to take a basket exposure to commodities and manage risks in a simple manner. If and when institutions such as fund houses are allowed to create and offer ETFs on commodity indices, this would be an opportunity for Indian investors to gain easy access to a new asset class, and thereby, enrich their investment portfolios.

**Features of some Global commodity funds**

| Strategy | Underlying commodities | Key Features |
|---|---|---|
| Active, Long only | Energy, Agriculture, Base Metals, Precious Metals, Livestock, Soft | Invest in commodities using derivatives through strategies like - relative value/ pairs trading, capturing curve volatility and uncorrelated alpha, Intra and across sector relative value |
| Passive, Long only | Energy, Agriculture, Precious Metals, Industrial Metals, Livestock | Invest in commodity-linked derivative instruments that track the return of a broad basket commodity Index Total Return |
| Active, Long-short | Precious Metals, Agriculture, Energy, Industrial Metals | Fund's objective is to provide total return of a benchmark broad basket commodity index.The fund seeks to achieve its investment objective by investing in derivatives and other commodity-linked instruments. |

## LETTERS TO THE EDITOR

### Railways must focus on safety first

Apropos of the news report "Jammu Rajdhani Express derails at New Delhi Railway Station" (*FE*, September 14), such a worrisome development, that too at the nation's premier railway station, does not augur well for the already poor image of the Indian Railways. This speaks volumes about our actual readiness to introduce the much talked about Bullet trains in India. But if one goes by the unprecedented poor and shocking safety record of the Railways, the moot question is: Whether India should still go ahead with the ambitious project even in the next 10 years? Railways should first think about the passengers' safety and ensure that all our existing trains run properly on the tracks. Needless to say, the recent spate in the train derailments only add to the woes of the Railways which seems to be devoid of any workable future game-plan to deal effectively with the same as each such accidents could largely be attributed to manual failure. However, it may not be prudent to expect any positive results on this front in the near future, too.

— Kumar Gupt, Panchkula

### Airbags are a must

Apropos of the recent edit "Uncertainty kills", whether the government makes it compulsory or not, auto-makers must show personal responsibility in incorporating a vital life-saving device like airbags in their vehicles. One cannot but recall the pioneering efforts of the internationally renowned American lawyer turned consumer activist Ralph Nader who, for the first time in the automobile history, got airbags and similar safeguards against accidents like seat belts, shatterproof windshields, padded dashboards, etc, made compulsory in American cars. The US passed the Traffic and Motor Vehicle Safety Act of 1966, based on Nader's seminal 1965 book *Unsafe at Any Speed* which exposed how cars were sacrificing occupant safety for the sake of looks and profits. All said, driving at safe speeds is the ultimate precaution one must take, failing which even airbags cannot save lives.

— CV Krishna Manoj, Hyderabad

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ILLUSTRATION: ROHNIT PHORE

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10TH YEAR OF GLOBAL FINANCIAL CRISIS

# Public sector banks still a drag for India

Bereft of adequate capital, PSBs can only manage to survive, not grow. Time is now opportune to reflect on how to immediately recapitalise

**THE "OFFICIAL" ONSET** of the global financial crisis is usually associated with the collapse of Lehman Brothers on September 15, 2008. Today, we enter the decadal year of the global financial crisis, and it is time to reflect on what went wrong and how the global banking and financial system has moved to safety. However, with a huge load of stressed assets on their balance-sheets, Indian banks, particularly public sector banks (PSBs), are still a drag on the growth potential of India.

There is no one single cause or reason for the global financial crisis of 2008. Many reasons are ascribed. There was a continuing imbalance in the "real" sector of the global economy: in the trade account, China (and some other Asian economies) and Germany had huge surpluses against advanced economies like the US and other European countries, and thereby accumulated foreign exchange reserves. These reserves created imbalances in these trade surplus economies and spilled into the capital accounts of advanced economies of the US and Europe.

Fault-lines were developing in the socio-economic fabric of the USA, as described by Dr Raguram G Rajan in his seminal book, Fault lines, due to stagnant income and increasing poverty. When politicians could not reduce poverty and inequality, they found abundance of money in the economy and devised schemes for banks to lend mortgage loans to the sub-prime borrowers. If they can't eat bread, "let them eat credit."

The persistence of capital flows into the advanced economies depressed yields or returns on investment and in "search for yield" financial engineers developed innovative products like securitisation, re-securitisation, credit default obligations, credit default swaps, and etc, on the mortgaged-backed securities.

The banks' business model underwent a change from "origin to hold till maturity" to "origin to distribute". Cheap liquidity available in abundance in the wholesale funding market encouraged banks to over-leverage. What was missing was capital, that too high quality, core equity capital in the banks' books. The regulatory requirement of common equity Tier 1 capital, of Basel I vintage (1988), was too meagre and did not keep pace with time. Banks indulged in capital arbitrage by keeping their trading exposures to mortgage-backed securities in the banking book, instead of the trading book where capital requirement was higher.

The corporate governance and executive compensation schemes of banks were poorly designed, which rewarded short-term performance over long-term achievement. The leaders of the financial world were lulled by the success of "financial engineering" and got carried away by "irrational exuberance" and could not see the "black swan" lurking at the door. Their immense faith in the capitalist system of "free markets" dissuaded them to "lean against the wind". When interest rates did turn, they were caught unprepared.

Credit rating agencies did a poor job while rating the sub-prime mortgage backed securities and the derivatives based on them. Did they "junk" themselves? And finally, what about the regulators? They were perhaps sleeping at the wheel. In focusing on individual financial institutions (micro-prudential regulation and supervision), they missed the macro picture. The financial sector had become too big in relation to the real sector and was perhaps beyond the capacity of the regulators.

"This time was different": The global financial crisis of 2008 was different from earlier crises on account of the roles played by the wholesale funding markets and the "shadow" banking system. Unregulated, or under light-touch regulation, they froze the funding markets when the crisis hit the financial institutions and there was a liquidity squeeze. The liquidity risk soon spread to the entire financial system and became a systemic risk going out of control. A liquidity crisis became the global financial crisis, nay, economic crisis, where the support extended by the authorities of advanced economies to their banks and financial system was almost a quarter of their GDP: the so-called "privatisation of profits and socialisation of losses".

Post-crisis, under the auspices of G20, the Financial Stability Board (FSB) and the Basel Committee on Banking Supervision (BCBS), several measures have been introduced to strengthen the financial regulatory system. The Basel III package envisaged improving the banking sector's ability to absorb shocks and reducing risk spill over to the real economy. The Basel III package includes micro-prudential regulation at individual bank level and overlay of macro-prudential regulation at system-wide level.

As a micro-prudential measure, Basel III raised the quality, quantity, consistency and transparency of the capital base of banks, with emphasis on core equity capital, to absorb losses during crisis like situations. The risk coverage of capital has been enhanced in respect of counter-party credit risk. A leverage ratio has been stipulated to supplement capital ratio and to contain build-up of leverage in the banking system. A liquidity framework to contain short-term liquidity risk (liquidity coverage ratio) and to contain structural liquidity risk (net stable funding ratio) has been introduced.

From macro-prudential or systemic risk regulation perspective, the Basel III leverage ratio would contain system-wide build-up of leverage that results in a destabilising unwinding process during stress and protects the perverse incentive to pile into low-risk assets, producing a systemic risk. Capital conservation buffer has been designed to create capital buffer, instead of distributing dividends, when times are good, and the same can be drawn down during times of stress. Counter-cyclical capital requirement has been put in place to protect banking system from periods of excessive credit growth, which is often associated with system-wide risk.

To avoid the moral hazard associated with "too big to fail" problem, a list of global systemic important banks (G-SIBs) has been drawn. The G-SIBs are required to self-insure themselves with additional capital, without depending the exchequer to bail them out during a crisis. Similar arrangements have been made for domestic systemic important banks (D-SIBs). The FSB and the BCBS have also put in place a Total Loss-Absorbing Capacity (TLAC) framework for G-SIBs, which will obviate the need for public money to rescues the big banks when they are in stress.

In collaboration with accounting standard setters, substantial progress has been made in devising a "expected loss" based loan loss provisioning, instead of the present "incurred loss" approach.

The Basel Committee has been monitoring the progress of implementation of Basel III package, to be fully the phased-in by January 1, 2019. In its latest Basel III Monitoring Report published on September 12, 2017, based on a sample data of 200 banks from different jurisdictions, as on December 31, 2016, Basel Committee has reported that on an average, banks have met with the new requirements.

India has also introduced the Basel III package with right earnest. However, the present stress in the balance sheets of our PSBs has considerably eroded their capital base. Bereft of adequate capital, PSBs can only manage to survive, not grow. Time is now opportune to reflect how to immediately recapitalise the PSBs in order to achieve healthy growth.

# Doubling farmers' income by 2022

RADHA MOHAN SINGH

Union minister for agriculture and farmers welfare


A seven-step path includes focus on agri-allied activities, expanding irrigation cover and risk mitigation

**TO IMPROVE THE ECONOMIC** condition of Indian farmers, prime minister Narendra Modi has set the target of doubling their income by 2022. The agriculture ministry is working on a seven-point strategy towards this end. The first step is to increase productivity. It means focusing on irrigation, and that is why we have increased the irrigation budget. India has 142 million hectares agriculture land, out of which only 48% is under institutional irrigation. With the objective of providing water to every field, Pradhan Mantri Krishi Sinchai Yojana was launched on July 1, 2015, and, to provide an end-to-end solution in irrigation supply chains, water resources, network distribution as well as farm level application. We have adopted a comprehensive approach, one that combines irrigation with water preservation. The objective is More Crop Per Drop. In addition, the aim is to complete pending medium and large irrigation projects on a priority basis in the next four years. Water harvesting, management, and watershed development projects have been put on the fast-track.

The second factor is effective use of inputs, which means increasing production through improved seeds, planting materials, organic farming, soil health card and other schemes. For the first time, a scheme has been launched for organic farming. Similarly, the government has curbed illegal use of urea and ensured its adequate supply through Neem-Coated Urea scheme. In addition, the Soil Health Card Scheme has helped reduce cultivation cost and increase production by curbing misuse of fertilisers. Farmers are also getting timely information and advisory services through new technologies such as space technology and online and telecom facilities via the Kisan Call Centre and Kisan Suvidha App.

> A number of reforms in agriculture marketing have been initiated; so far, 455 mandis have been linked to e-NAM

The next critical factor is reducing post-harvest losses. One of the biggest problems of farmers is storage after harvesting; as a result, they are forced to sell their products at a lower cost. Therefore, the government is encouraging farmers to use warehouses and avoid distress sales. Loans against negotiable warehouse receipts are being provided with interest subvention benefits. The focus is on storage facilities and integrated cold chains in rural areas.

Value addition is being encouraged as a critical factor for augmenting income. The government has launched the Pradhan Mantri Kisan Sampada Yojana. Under this, food-processing capabilities will be developed by working on forward and backward linkages of agro-processing, benefitting 20 lakh farmers and creating employment opportunities for about 5 lakh.

In agriculture marketing, The electronic-National Agriculture Market has been launched with three reforms and so far, 455 *mandis* have been linked to it. Online trading has begun on various *mandis*. In addition, a model APMC Act has been circulated, which includes private market yards and direct marketing. Farmers are also being organised as Farmer Producer Organization. This helps them achieve economy of scale and increase bargaining power.

The Pradhan Mantri Fasal Bima Yojana (PMFBY) helps reduce the possible risks. The scheme is a shield for farmers' income. The lowest rate has been fixed for kharif and rabi crops. Maximum rate is 2% and 1.5%, respectively. The scheme covers standing crops as well as pre-sowing to post-harvesting losses, and 25% of the claim is settled immediately online. Under PMFBY, many states are using remote sensing technology and drones to estimate losses and settle claims. To reduce climate change impact, various tolerant species and animal species have been developed. Contingency plans for affected districts have also been prepared.

Focus on agri-allied activities is critical. We are focusing on horticulture, dairy, poultry, beekeeping, fisheries, white revolution, blue revolution, agroforestry, integrated farming and rural backyard poultry development to increase the income of the farmers. We will increase the income of farmers through allied activities. Partially, it will be done through poultry, beekeeping, animal husbandry, dairy development, and fishery. We are encouraging farmers to utilise uncultivated areas for peripheral and boundary plantation to grow trees for wood and to produce solar cells. We are also emphasising on horticulture, agro-forestry, and integrated agriculture.

# Price controls are bad medicine

It will cause reduced investment and shortage of drugs & devices; the long-term solution is improving quality of govt hospitals


RITESH KUMAR SINGH

Corporate economist based in Mumbai. Views are personal

**AFTER CAPPING THE** price of coronary stents in February, the National Pharmaceutical Pricing Authority (NPPA) imposed price control on orthopaedic implants on August 16 to "check overcharging and unethical profiteering and make healthcare affordable." This follows a government notification on June 29 that declared 15 widely-used medical devices including balloon catheters, heart valves, disposable syringes, oxygen masks, urinary bags, and intraocular lenses as "drugs" under the Drugs and Cosmetics Act, 1940. That is the first step towards controlling their prices. However, it would be interesting to analyse if imposing price caps would end price-rigging and profiteering by unscrupulous private hospitals.

Private hospitals are found to be charging up to 500% of the actual cost for life-saving medical and surgical devices. That jacks up the overall cost of healthcare services and makes it unaffordable to many in a country where out-of-pocket medical expenses are as high as 70% of the total. Thus, it makes sense to impose price control.

However, the imposition of price caps may choke the supply of life-saving medical devices and discourage their production locally. Subjecting major bulk drugs to price control vide the Drugs Price Control Order, 1995, led many pharmaceutical companies to gradually move out of production that had a cascading effect on the supply of formulations made from price-capped bulk drugs. It's no secret that India is now heavily dependent on the import of bulk drugs and active pharmaceutical ingredients (APIs) from China.

Post the imposition of price cap on stents, many suppliers threatened to stop manufacturing and importing coronary stents, though the government momentarily forced them not to do so. However, it's safe to conclude that India may have to rely even more on imports of price-capped medical devices. As the latest innovations are expected to be expensive, price caps will induce the import of low-quality devices that will ultimately hurt patients. Moreover, it can also dampen the prospects of India's fast-growing medical tourism industry. Worse, it may induce nationals who can afford to go abroad for medical treatment.

India's healthcare services sector is an under-supplied industry. Private healthcare providers account for over two-thirds of all patients, as overcrowded and underfunded government hospitals are always short of beds, doctors, devices or essential medicines, as evident from the death of over 70 children in BRD Medical College Hospital Gorakhpur.

There's always a long waiting list for critical surgeries and a patient needs influence (or a little help from touts) to jump the queue. As a result, patients either go to private hospitals if they can afford or suffer from deteriorating health. Thus, it's the appalling state of government hospitals that forces even the poor to go to private hospitals.

There is no serious competition to private healthcare providers from government hospitals. Besides, the market for healthcare services is characterised by imperfect competition where the seller knows more than the buyer who can't shop around and bargain for the best deals, especially during medical emergencies. That puts patients (poor or rich) at the mercy of private hospitals.

This encourages rampant unethical business practices by unscrupulous hospitals, starting with overcharging to performing unnecessary operations or prescribing expensive medicines or diagnostic tests. Such practices are common even in developed countries. However, the extent of medical malpractice and price-rigging is unreasonably high in poorly-regulated India's healthcare sector. Thus, some form of government intervention is needed to rein in private hospitals. However, imposing price controls is too simplistic a solution to work.

The major reasons for overcharging or unethical profiteering by private healthcare providers are lack of competition and information asymmetry, i.e. the seller knows more than the buyer. That can't be tackled by imposing price control, which may bring many unintended consequences such as reduced investment and eventually the shortage of life-saving medical devices.

Roughly 60% of medical and surgical devices used in India are imported. Unlike medicines, India's underdeveloped indigenous medical device industry can't really supply the country's ever-growing requirements. Moreover, imposing price caps on medical devices will induce private hospitals to raise the charges of procedures/fees/bed rentals (to compensate for lower margins on devices), unless the government wants to impose price caps on every medical item.

A long-term and non-market-distorting solution to overcharging or unethical business practices by private hospitals is to improve facilities in government hospitals. If relatively cheaper and quality options are available, patients will automatically opt out of unscrupulous hospitals. That would require an increase in public spending on healthcare—a meagre 1.4% of the GDP goes towards healthcare (compared to 3% in China or 4.3% in Brazil)—and India needs to raise it to at least 2.5%. That would also require cutting red tape, reining in corruption and fixing accountability in government hospitals, and agencies and departments controlling them.

The government should instruct all healthcare providers—private public—to display all charges and fees for all kinds of treatment, including prices of medical devices and instruments, on their websites, so that the buyers of healthcare services can decide where to go and which facilities to use. This will reduce information asymmetry and improve transparency.

Though overcharging and profiteering is a serious problem, imposing price controls is a bad medicine that will have many side-effects, including reduced investment and shortage of life-saving medical and surgical devices in the country. The long-term solution lies in improving the quality of government hospitals.