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Crisis for IBC

Secured creditors' rights must not be diluted

Two recent judgments relating to the rights of creditors are shaking the financial markets in India. They have the potential to not just stall the working of the Insolvency and Bankruptcy Code (IBC), but also to dry up the pool of potential investors in stressed assets in India —and, indeed, to clog up the working of the credit markets altogether if they go down as a precedent to be followed. These decisions are by the National Company Law Tribunal (NCLT) in relation to the dues to creditors of the troubled Infrastructure Leasing and Financial Services (IL&FS); and by the National Company Law Appellate Tribunal (NCLAT) with respect to the sale of Essar Steel.

The NCLAT has approved ArcelorMittal's bid to buy Essar Steel for ₹42,000 crore — but has overruled the Committee of Creditors (CoC), which had set aside only 10 per cent of that amount for Essar's operational creditors. The NCLAT has instead said that just under 40 per cent should go to the operational creditors. Banks with exposure to Essar Steel have, at one stroke, seen their payout diminish. In effect, the loans given by the banks — secured creditors — have been put on par with operational creditors. Meanwhile, the NCLT directed that provident funds (PFs) that had lent money to IL&FS, even if not secured, should be treated on par with secured creditors, because the beneficiaries of PFs deserve special treatment. Here, secured and unsecured creditors are being treated equally.

This strikes at the very root of modern finance — which is structured so that multiple risk-return profiles are made available to investors. Secured loans receive a lower interest rate, in return for being first in the line for payouts if something goes wrong. The NCLT and NCLAT have refused to abide by this principle. The Essar Steel creditors have appealed to the Supreme Court (SC), and it is to be hoped that the SC will keep this principle, which underlies the letter and spirit of the IBC, in mind. While it is unfortunate that PFs might make a loss on their exposure to IL&FS, for example, it is up to the guarantors of the PFs in question to ensure that the beneficiaries do not suffer.

If the legal system seeks to protect groups of individuals at the cost of undermining the credit architecture more broadly, it would be counterproductive. Already, in relation to various real estate matters, apartment buyers are being treated on par with financial creditors — which has had a predictable negative effect on credit to real estate in India. If such thinking is extended, as it has been under these two decisions, then not only will foreign funds refuse to invest in stressed assets, but the entire IBC system, predicated on the rights of the CoC to make decisions about the future of the company, will break down. Effective interest rates will also skyrocket, which will hurt all future investments. Besides, financial creditors would rather enforce security at the first sign of financial distress in a firm or choose to vote for liquidation, since in both cases they would stand to make higher recoveries as opposed to a resolution plan under the NCLT. This is like incentivising liquidation. Both in terms of natural justice and consequentialist ethics, there is good reason to re-examine these decisions.

Shooting for the moon

It's time ISRO was given more resources

The postponement of the Chandrayaan II launch less than an hour before the scheduled lift-off means yet another delay in the moon exploration plans of the Indian Space Research Organisation (ISRO). This is the seventh time this mission has been postponed, putting it six years behind the original schedule. The underlying reason for that delay, and for previous delays in the development of key technologies, such as the cryogenic engines of the GSLV series is, essentially, lack of resources. That, in turn, points to the misplaced priorities of policymakers.

It is often proudly claimed that ISRO is the most frugal of space agencies, functioning on budgets dwarfed by its competitors. It is seen by policymakers as a cost centre that buttresses India's soft power, and it is budgeted for accordingly. The agency will receive ₹11,538 crore in 2019-20. The Chandrayaan II mission will cost a little less than ₹1,000 crore — that is roughly one-seventh the cost of the failed Israeli Beresheet mission, with comparable objectives.

This parsimonious attitude needs review. ISRO has made very significant contributions to India's communication and navigation systems, and weather forecasting. It could not only contribute more in multiple areas, such as renewable energy, road design and water conservation but also generate large revenue by competing more aggressively in the global satellite market.

ISRO should, therefore, be seen as a potential profit centre, which can more than pay for itself. To that end, it should not only be allocated larger budgetary resources but also be allowed to raise funds from the market like other public sector undertakings. Earlier attempts to monetise ISRO's research & development (R&D) skills through the commercial arm, Antrix, were not very successful and were mired in controversy after the Devas deal. Creating New Space India Limited (NSIL), a PSU to commercially exploit R&D, market satellite launches, and so on, is a welcome development. The NSIL will look at the transfer of small satellite technology to the industry, manufacturing of Small Satellite Launch Vehicles (SSLV) in joint ventures and production of Polar Satellite Launch Vehicle (PSLV). Ideally, the NSIL will be able to identify other sectors where ISRO can contribute to profitably.

The agenda for Chandrayaan includes a soft landing on the moon's South Pole, followed by exploration by a robotic rover, which will conduct various experiments. If all had gone well with the launch on July 14, the landing would have occurred on September 6-7. However, the ISRO quite wisely now says that it will not announce a new launch date until it has fixed the technical problem that caused the abort.

Delays caused by technical hitches in such complex missions are not unusual. There was also a long delay to the development of cryogenic rocket engines for the GSLV after sanctions kicked in post-Pokhran II. ISRO's intention of undertaking manned missions in future will involve solving even more complex problems to ensure that it keeps human beings healthy in airless, high-radiation environments with variable gravity. These technical challenges will require many man-hours to solve. The payoffs could also help to improve health-care, food/water preservation, and recycling technologies.

Given that India possesses a large pool of scientists with the requisite skill sets, R&D in aerospace can definitely be speeded up by giving ISRO the resources to deploy more skilled manpower to tackle these problems. Faster development of technology would also allow it to become self-sustaining.

ILLUSTRATION: AJAY MOHANTY

India's upcoming G20 presidency

New Delhi must guard against the world's premier multilateral economic forum being hijacked by bilateralism

ALOK SHEEL

The G20 is by consensus the premier multilateral forum for global economic cooperation. The 17th G20 Summit will be held in India in 2022, easily the most high-powered summit ever hosted here. Leaders of all systemically important countries — including the full complement of G7 and BRICS — are expected to be present. It would be the Indian prime minister's place in the sun, chairing a meet flanked, inter alia, by the US President, the British Prime Minister, the German Chancellor, the President of the European Union, the Chinese President, the Japanese Prime Minister, the President of Russia, with the chiefs of major multilateral bodies like the International Monetary Fund (IMF), World Bank and the UN in attendance. The leaders are expected to sign up to a document likely to go down in history as the New Delhi Declaration, including a "New Delhi Action Plan".

What does hosting a G20 Summit successfully entail? There is first the logistical and security nightmare of hosting all influential global leaders in one location at the same time. It is understood that the summit would be held in a new convention centre under construction in Delhi. It is, however, not essential that the summit be held in Delhi. After the first few summits, these have been mostly held in convenient resorts, such as Cannes (France), Los Cabos (Mexico), and the last in Osaka. Apart from an appropriate convention complex, security, air and road traffic control, you need adequate numbers of five-star rooms to accommodate so many high-powered delegations.

The G20 took a conscious decision not to set up its own secretariat, for fear of the institution becoming captive to an international bureaucracy, such as in the IMF and World Bank. It wanted leaders to retain control of the summit process. The annually rotating Chair is expected to inject fresh energy and pilot the summit. Institutional continuity is provided through the troika comprising the current, previous and upcoming Chairs. India will be in the troika between 2021 and 2023.

It is the Chair's prerogative to choose two to three special invitees to the summit. Although not a part of the G20 by convention, Spain has attended all G20 Summits. There is also a special invitee from Africa. That still leaves India the discretion of inviting a SAARC country of its choice as part of its outreach.

The G20 was set up in the wake of the Asian Financial Crisis in 1999 at the level of Finance Ministers and Central Bank Governors (FMCBG). This was overlaid with a 'Sherpa' channel when it was elevated to Summit level in 2008. The Sherpa is the Leader's point person responsible for agreement on the summit declaration.

The first three summits — at Washington DC, London and Pittsburgh — were all about firefighting the rampant global financial crisis. After declaring victory in Pittsburgh — "It worked" — the G20 turned its attention to structural, non-crisis related issues, such as reform of financial regulation, global imbalances, and growth. India co-chairs, along with Canada, the G20's flagship working group, the Framework for Strong, Sustainable, Balanced and Equitable Growth, since its inception at the Pittsburg Summit. Several ministerials were also added, such as those of development ministers, environment ministers, trade ministers, agriculture ministers etc. All these work streams feed into the G20 Summit Declaration. There are also a growing number of non-governmental processes, such as the T (Think Tank) 20, W (Women) 20, Y (Youth) 20, and so on.

The Chair is expected to pilot the multiple work streams that currently drive the G20 through its own secretariat. This includes, inter alia, drawing up the annual work programme and hosting the meetings, culminating with the summit. A summit where all the major world leaders sign up to a consensus document has a long lead time, normally more than a year. Saudi Arabia, the summit host in 2020, set up a secretariat way back in 2018. With a new government now in place, it is time India initiated this process.

It is customary for the Chair to set three or four priorities for the year and inject new work streams to leave its own imprint on the G20 process. India would need to ponder what priorities it needs to set, and what ministerials it wishes to host, under its watch. While these should reflect India's own domestic interests, a successful summit also needs buy-in from at least the biggest players, namely the US, Germany (on behalf of the European Union) and China.

The Indian Sherpa shepherding this process needs the stature that commands respect of the global peer group, apart from the confidence of, and easy access to, the Prime Minister. For such a high-profile summit, the Sherpa should ideally be part of the Prime Minister's Office but could also be in the Ministry of External Affairs (MEA). A serving or retired bureaucrat with the necessary experience is desirable but not essential. Be that as it may, strong dedicated teams are required in the MEA (Sherpa process) and Department of Economic Affairs (FMCBG process). The MEA would need to liaison effectively with the embassies of G20 countries for better communication, and especially for selecting participants for NGO processes.

The danger is that if there is no strong buy-in from major G20 players, extraneous extant exigencies not on the official agenda could hijack a G20 Summit, especially when hosted by a non-G7 country. The crisis in Syria effectively hijacked the St Petersburg Summit. Brexit, the Khashoggi affair, and bilateral trade issues overshadowed the Buenos Aires Summit. The prospects of a Trump-Xi trade deal dominated the recently concluded Osaka Summit.

With the world's top leaders aggregated in one place, bilaterals and 'pull-ins' have always been a feature of G20 Summits. But the world's premier multilateral economic forum never faced the existential threat from bilateralism as it does today. The litmus test of India's G20 Summit might well be whether it is remembered for the New Delhi Declaration/Action Plan, or for some high-profile bilateral deal/pull-in between superpowers.

The wrieter is retired IAS officer and currently RBI Chair, ICRIER. He anchored India's G 20 delegations during the first seven G20 Summits.

Trump is slowing US economic growth

ROBERT J BARRO

For some time, the four horsemen of US macroeconomic policymaking have been taxation, regulation, trade, and infrastructure. Having studied the first in detail, I have found tax cuts to be a positive contributor to economic growth. Though I have considered the second area in less detail, the evidence suggests that regulation is, at best, only a minor contributor to growth. The third area is very important, which is why today's trade tensions are so worrying. The fourth area exists only in rhetoric: an infrastructure programme is currently not a part of the macroeconomic policy repertoire.

In the first area, I estimate that the 2017 tax legislation added 1.1 per cent per year to the United States' GDP growth rate for 2018-19. Of that, 0.9 percentage points reflected the reduced tax rate on individuals, whereas 0.2 percentage points derived from the rate cuts and improved expensing provisions for businesses. While the growth-enhancing effect of the tax cuts for individuals is not expected to continue beyond 2019, the impact of the corporate-tax reform will likely persist for some time to come.

As for the second horseman, there is some indication that the expansion of federal regulations has begun to taper off, after undergoing a long period of growth. As of 2017, RegData, which tracks the number of words relating to constraints on economic activity in the Federal Register, shows that new regulations have plateaued. The regulatory burden on business and economic activity is no longer rising, but it is not diminishing, either.

Likewise, the World Bank's Doing Business profile for the US, which offers a broader measure of government regulation based on an average of 10 indicators, show no recent progress. The US rose from eighth place in 2016 to sixth place in 2017 in the global ranking, only to fall back to eighth in 2018. And, putting aside relative performance, a cardinal representation of the underlying indicators shows virtually no change in the 2016-2018 period.

As many other economists have noted, US President Donald Trump's trade policies are a major concern. The administration's trade agenda is driven by the discredited mercantilist idea that selling stuff (exports) is good and buying stuff (imports) is bad. The irony is that Trump and some of his top trade advisers share this misguided view with the Chinese.

Indeed, the Trump administration is correct that the Chinese have long restricted imports and foreign investment (while engaging in technology theft, either directly or by compelling transfers). But the tit-for-tat exchange of import tariffs between the US and China over the past year is bad for both countries. Many assume that the trade conflict will hurt China more than the US, given that China exports far more to America than America exports to China. But the loss of Chinese imports will impose a major burden on the US economy.

Trump's views on tariffs remind me of a speech that Ronald Reagan gave at Stanford's Hoover Institution before he became president. Reagan argued that tariffs on steel and other goods were justified on national-security grounds. His reasoning, criticised by audience members, was almost the same as Trump's today. Yet, to justify his tariffs, Trump has gone even further, equating national security with economic security. The best way to invalidate that argument on legal grounds, then, is simply to have an economist show in court why tariffs are bad for economic security.

The broader problem is that Trump seems to have a personal affection for tariffs, partly because he thinks they raise revenue, and partly because he thinks they raise GDP (by curbing imports, which are then magically replaced by domestic production). This challenge does not admit of an easy remedy. Some have called on Congress to reassert its authority over tariffs — at least by limiting the national-security argument. But this could have unintended long-term consequences, given that presidents since the 1930s have tended to be far more supportive of free trade than have members of Congress, each of whom represents the interests of a narrower constituency.

The hope now is that mutually harmful tariffs will lead to an agreement whereby China liberalises its trade policies, at which point import barriers will be removed. But though this — to add irony to irony — would benefit China more than the US, the situation is fraught, with uncertainty about the outcome fuelling the volatility of global stock markets. And whatever happens with China, we still have to worry that Trump will impose tariffs on Mexico, Europe, Japan, and so on.

As for infrastructure, the potential benefits to US productivity from increased investment are real. Yet nothing has happened. The situation is best encapsulated by an April meeting between Trump and congressional leaders. According to media reports, Trump began by proposing to spend $1 trillion on infrastructure, whereupon the Democrats countered by suggesting $2 trillion. Trump apparently agreed to that with little hesitation. All in all, the exchange confirms, once again, that both parties have come to regard government spending as a free lunch, at least when it is financed by debt or the creation of new money. Perhaps it is actually for the best that "Infrastructure Week" never goes anywhere.

Given the state of US macroeconomic policy, it is not surprising that the Federal Reserve Bank of Atlanta's latest *GDPNow* report forecasts second-quarter GDP growth of 1.3 per cent, down from 3.1 per cent in the first quarter. The 2017 tax reform would still be promoting economic growth if not for the escalating trade tensions. Sadly, a growth rate of close to 3 per cent for 2019 no longer looks likely.

The writer is Professor of Economics at Harvard University and a visiting scholar at the American Enterprise Institute. His latest book, with Rachel McCleary, is The Wealth of Religions: The Political Economy of Believing and Belonging.

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Short shots

KITABKHANA

T C A SRINIVASA-RAGHAVAN

Last month I wrote that book-wise at least, the last six months have been very lucky for me because I have constantly discovered new authors and some very nice books. I am happy to report that my luck hasn't run out, as I found out earlier this month.

I came across, totally by accident, a book of short stories by none other than the youthful principal economic adviser to the finance ministry, Sanjeev Sanyal. I knew he had written some books on rivers and seas. But I had no idea he has written a book of short stories.

It was while browsing on Amazon that I saw his book on the usual menu of offers. When I saw the price, I decided to take a flutter. It was a good bet, ₹250 well spent because as a connoisseur and writer of short stories, I can say this: Mr Sanyal does a damned good job of it. I hope he continues to write them.

The book is called *Life Over Two Beers,* which is also the title of one of the stories. It could have been called anything else but after rivers and oceans I suppose beer is not a bad option.

Mr Sanyal writes with a smoothness that suggests polishing and re-polishing. There are absolutely no superfluous words. Thus, the sentences are short, which is an absolute *sine qua non* for a short story.

The stories move along until (I think) Mr Sanyal gets bored and decides to stop them. It then comes to a gentle halt. This is as difficult as bringing a Bombay suburban to stop just so.

I would strongly recommend this book to everyone not just for the quality of writing but also for its insights and observations on daily life, especially of the upper middle class in Delhi.

I saw the phrase Khan Market Consensus in one of the stories, and since the book was published last year, I wondered briefly if the prime minister had also read the story. No? Well, never mind. He is a busy man.

An elite group

Mr Sanyal belongs to an elite group. Economists who write stories are rare. Of the 200,000 or so economists that infest this planet, to the best of my knowledge, only five have written them.

The granddaddy of them all was John Kenneth Galbraith who wrote two I think. I have read one of them. I now plan to get the other.

In the 1970s, two professors, one of them from Harvard, decided to write murder mysteries. They wrote three such novels over the next 20 years under the name Marshall Jevons.

I bought them at considerable expense but my son, who is an economist, has made off with them. As Oscar Wilde said about economists, he knew their price but I am sure not the value. I will have something to say if he loses them.

Kaushik Basu has also ventured forth in the literary direction. But he has written a play not a novel. But I am sure he will one of these days.

Then there is Bibek Debroy. Apart from all that heavy lifting translating Indian epics, he has also written a novel and a book of limericks. I have not read either. I am now waiting for Surjit Bhalla to write one. He is bound to take up the challenge and come up with a bestseller.

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Perfect entertainment

Coming back to short stories, as even Mr Sanyal discovered, the market for them seems to have disappeared, in English at least. There is simply no one who will agree to publish them unless you are a Bollywood celebrity or, dare I say it, a principal economic adviser.

Mr Sanyal says he wants to revive the art of writing short stories. He can start by recommending mine to a publisher.

Even this newspaper — which happily publishes my other drivel — has refused to publish them.

Mr Sanyal is absolutely right and not just for literary reasons. The short story is a brief entertainment that is over in three to thirty minutes. In this age of Twitter, Facebook, news notifications and other distractions, it is perfect for online textual entertainment that should be offered by newspapers and magazines.

You don't think so? Just look at how well English translations of short stories in Indian languages sell.