Economy This Week (6th May to 19th May 2019)

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1. Govt plans sectoral ETFs

This news item is taken from Business Standard (13th May 2019).

- DIPAM (Department of Investment and Public Asset Management) has planned to launch 3 sectoral equity exchange traded funds (ETFs) - Banking, Energy and third one in metal and commodity sector
- These would be attractive to investors as investors wish to invest in specific sectors and will also help the government in meeting the ₹ 90,000 Cr target in disinvestment
- The banking sector ETF is expected to comprise shares of some of the 19 listed state-owned banks
- The energy ETF is expected to have shares of state owned companies in oil and gas, and power sector
- The metals and commodity ETFs basket could comprise shares of companies like Coal India, Steel Authority of India, National Aluminium Company etc
- Currently there are two ETFs which are offered by the govt
    - CPSE ETF comprising 11 stocks (heavily skewed towards energy and commodity sector), managed by Reliance AMC
    - BHARAT 22 ETF draws the shares from six sectors, managed by ICICI Prudential AMC

2. India has restrictive market barriers

This news item is taken from The Hindu (8th May 2019).

- While US is India's largest export destination, India is 13th largest export destination for US
- India's exports to US account for 20% of the total exports from India
- India has a trade surplus with US
- The American technology and expertise would play an important role in promoting the growth in India, the US companies are facing significant trade barriers (both tariff and non-tariff)
- India on an average imposes a tariff rate of 13.8% and remains one of the highest in the world and this has been one of the stress points between India and US
- These issues were being addressed under the US-India bilateral dialogue
- Other sectors that were mentioned - the prices controls on medical devices and pharmaceuticals, tariffs on the electronics and telecommunications

3. Need to promote investment in infrastructure

This news item is taken from Business Standard (17th May 2019).

- For the 11th FYP, the infrastructure investment rose to 7% of GDP, compared to 5% in the previous FYP. Major reason for this has been the increase of investment by the private sector. The investment by the private sector rose by 15% compared to the previous FYP
- Having seen this kind of growth in investments, it was not sustainable as it encountered issues such as land acquisition skewed risk allocation, myriad of regulatory clearances from multiple agencies,

dominant role of commercial banks played in infra financing. That's why the infrastructure investment by the private sector post 2013 slipped back and remained at 5%. The private investment target was set at 48% between 2013 and 2018 and the investment was nowhere close to it. This decline in the private sector was bridged by the public sector in the last few years

- Going forward this kind of investment by the public sector cannot be maintained because of the fiscal constraints. On the other hand both the major national political parties have pledged to ramp up the investments to the tune of ₹ 1 lakh cr in the infrastructure by 2024, which means that the private sector investments have to increase. For this to happen, the govt should address the structural issues
- The govt had asked the Vijay Kelkar committee to give recommendations relating to PPP and many of those recommendations (given in 2015) are equally applicable today
    - Recommended setting up of PPP Project Review Committee and Infrastructure PPP Adjudicatory Tribunal (IPAT) which would decide if the terms of the projects need to be revisited if the economic context or conditions had changed. This would provide for renegotiating the agreement
    - Had highlighted the need of the independent sector regulators (in case of Railways, Indian Railways is the policymaker, developer, regulator all rolled into one and this creates conflict of interest; it holds true even in case of the road sector. In sectors where the regulators are present they are not completely independent)
    - Amending the PCA - Prevention of Corruption Act 1988 - so that genuine commercial errors of judgement by the officials are not penalised
    - Equitable Allocation of the risk between the government and the private players. The risk allocation has to be clearly specified in the agreements

4. Resolving banking crisis

This news item is taken from The Hindu (11th May 2019).

- The new govt has to resolve the banking crisis but for that it first needs to understand the cause of the crisis
- The NPAs have increased from 2.26% of gross advances or being about ₹ 5.6 tn (in 2007-08) to 11.2% of gross advances or ₹ 10.3 tn (in march 2018). Of this 86% amounting to ₹ 8.9 tn is from the PSBs
- The origin of this lies in the credit boom during the years from 2004-05 to 2008-09. In this period the global and domestic economy was booming and the commercial credit or non-food credit doubled. The corporate sector borrowed for investment purposes, believing India would continue to grow at 9%
- Thereafter many things went wrong - land acquisition, environmental clearances etc as a result of which many of the projects got stalled, the cost of the projects soared. Along with this, there was global financial crisis followed by a slowdown. Revenues of the companies were affected, policy rates were increased which increased the cost of capital, there were outflows of dollars resulting in rupee depreciation which meant the corporate borrowers who had borrowed (from external market) had to cough up higher amounts etc
- In 2014-15, RBI conducted AQR (Asset Quality Review) to find the true situation of the NPAs. The NPAs in FY16 almost doubled over the previous year
- Higher NPAs led to higher provisioning by the banks, which not only affected the profits of the banks, it also eroded the capital
- Some have recommended privatisation of PSBs as a right step forward to overcome this issue. If the figures are looked into, the private sector banks also suffer from the menace of NPAs. banks such as ICICI and Standard Chartered have reported NPAs of 9.9%, 11.7% NPAs respectively. The private banks also are a part of consortia which have given huge loans and they have turned NPA
- The reason why the PSBs account for higher NPAs
    - They had very high exposure to the affected sectors - mining, iron and steel, textiles, infrastructure, aviation. These sectors accounted for 29% of the advances and 53% of the

stressed assets in PSBs (dec 2014); and the PSBs accounted for 86% of the loans for these sectors

- Plan to prevent such crisis - some reforms for immediate and medium term should be implemented
    - Immediate
        - Banks must accept the losses/haircuts on these stressed assets without any fear of investigation or harassment by other agencies
        - A Loan Resolution Authority could be appointed to expedite the resolution of NPA issue in lead banks (IBA - Indian Banks' Association - has already appointed a six-member panel)
        - Government should infuse the capital in one go rather than providing it in instalments
    - Medium term
        - RBI needs to develop better tools to monitor macro-prudential indicators. It essentially needs to look into formation of credit bubbles
        - Actions to strengthen the functioning of banks in general and PSBs in specific
        - Risk management in PSBs needs to improved
        - Succession planning needs to improve