ETW 30th Sep to 13th Oct 2019

Need to upgrade deposit insurance (LM 30/9/19)

- The issue of PMC (Punjab Maharashtra Co-operative bank) has put into limelight the need to revise the deposit insurance and depositor protection
- In case of the deposit insurance, depositors would be receiving certain amount in case the bank is under liquidation (this will be paid to them before the other parties)
- In case of India depositors will be covered up to ₹ 1 lakh (was ₹ 30000 earlier, was increased in 1993)
- This insurance amount needs to be revised
    - India fares poorly when compared with other Asian peers
        - In the case of the Philippines it is up to 500000 pesos ($9500) per depositor
        - In case of Thailand it is up to 5 mn baths ($1,60,000) per depositor
        - In the case of China, it is up to 500000 yuan ($70000) per depositor
        - At ₹ 1 lakh per depositor, India provides insurance of up to $1400
    - Indian economy has changed drastically; the per capita income has increased. A substantial part of the incremental savings of the individuals have been flowing into the banks. As per RBI data for FY17, bank deposits comprised of 66% of the financial savings of the households
    - The size of bank accounts having over ₹ 1 lakh have jumped. 90% of the individual bank accounts had a deposit of up to ₹ 1 lakh and by 2018 this has dropped to 62%. This means a substantial number of these accounts have large deposits
    - Indian economy is a bank led economy and a substantial savings from the households keep flowing into the banking sector. Hence the households have an implicit trust in the banks. If the deposit insurance is increased, then it will provide much more comfort and increase the trust

India set to lose major WTO dispute (LM 30/9/19)

- A WTO dispute settlement panel has upheld one of US complaints that the export subsidies given by the govt are violating the provisions of SCM (Subsidies and Countervailing Measures) under WTO
- The 3-member panel has stuck down Indian export schemes stating that India is not supposed to provide such subsidies as its GNI (Gross National Income) per capita has crossed $1000 per annum
- This is supposed to be released by 10th October. Once released the parties involved can challenge the ruling within 30 days before an appellate body (is the highest court for resolving global disputes). If the panel also upholds the ruling, then India will have to withdraw these schemes
- Some of the schemes that would get affected are MEIS (Merchandise Export from India Scheme), EPCG (Export Promotion of Capital Goods), SEZ (Special Economic Zones), duty free imports for exporters etc

- The violation cited is article 3.1(a) of SCM, under which the countries with GNI per capita of over $1000 per annum are not entitled to provide export subsidies that are contingent upon export performance
- India in 2015 and 2017 had announced that it would discontinue these export subsidies soon, but has continued to provide the export subsidies

Risk to state govt finances (BS 3/10/19)

- GST collections for the month of September have dropped to 19-month low of ₹ 91916 Cr
- A lower GST collection, along with lowering of corporate tax rates leading lower corporate tax collections and the slower growth in direct taxes will affect the finances of central govt as well as state governments
- The fiscal pressure on the states would be very high as they spend one and a half times more than the centre and also account for over two thirds of the general govt capital expenditure
- The recent report of RBI on state finances has noted that
  - The states have budgeted for a fiscal deficit (FD) of 2.6% of GDP this year (last year it was revised to 2.9%). Though it is notable that the FD has been lower than 3%, the states have cut down the quality expenditure and revenue expenditure has been higher than budgeted
  - For 2018-19 the states had to adjust the FD slippage 34 bps downward because of lower receipt collections, higher revenue expenditure on account of loan waivers and income support schemes. All of this reduced the capital expenditure. This lower capital expenditure will not only hamper the growth in the medium term, but also hamper the revenue mobilisation of the states
  - No doubt that the states will be compensated in case of lower GST collections but it has to be kept in mind that this arrangement is not permanent
  - The debt at the state level has been increasing in the last couple of years and stands at 25% of GDP. The report has stated that India has one of the highest debt to GDP levels at sub national levels among its peers. The report notes that if only this debt is considered then it is sustainable but if the outstanding guarantees (states give guarantees for the PSEs borrowings) are taken into account then the debt becomes unsustainable
  - If the debt to GDP has to be brought down to 20% by 2024-25 (as recommended by N K Singh Committee) then the revenue receipts have to increase by 14% every year
- Overall the states have adhered to the FD targets but if the slowdown continues then it may affect the revenues which may spiral into lower expenditure leading to the vicious cycle. Hence there is a need for the states and centre to come together to push up economic activity, increase tax compliance, prioritise capital expenditure etc

Limits of what RBI can do for the economy (LM 7/10/19)

- Last week RBI cut the policy rate or repo rate for the fifth consecutive time. Since February this year, the repo rate has been slashed by 135 bps by the central banker. Now the central banker will be lending to commercial banks at a rate of interest of 5.15%

- Despite RBI reducing the repo rate, there are still doubts about its impact on expanding the credit in the market. As it has been seen that despite RBI reducing the repo rate by 110 bps between February to August this year, the lending rates were reduced by an average of 29 bps
- To ensure efficient monetary policy transmission the banks have been asked to price some of their loans under external benchmarks from 1st October. The efficacy of such a directive from the central banker has been disappointing in the past because many of the banks are owned by the govt which reduces the competition in the market, there is a poor record of risk assessment, high NPAs, acute scarcity of low cost funds (as the govt offers higher interest rates on its small saving schemes) etc
- The slowdown in the economy may have more to do with lower consumer demand rather than the interest rates on the loans. As with reduction of repo rate the loan may become cheaper but the businesses would invest in increasing their production if there is higher aggregate demand
- While RBI on one side has been reducing the lending rates, govt on the other side has announced a host of measures, the most important being a reduction in the corporate tax rate. This will not put money in the hands of the consumers which would have increased the aggregate demand
- Perhaps the govt would be in a better position to address the slowdown if they can address the demand issue by reducing the personal income tax rates