

Business Standard

VOLUME XI NUMBER 281

Correction scenario

With the huge surge of dollars into the country showing no signs of abating (reserves grew by \$8 billion last month and by 1.9 billion in the first week of this month), some alarm bells have already begun ringing at the prospects of what would happen if the money begins to flow out, as it should whenever US interest rates rise. Traditional arguments that foreign institutional investors will not pull out since this will cause a huge fall in the Sensex and therefore in their own asset values, may not hold water since FII trades are often programme-driven, which is why the herd tends to move in the same direction. If perceptions about India change—and who is to say that things will always look rose-tinted—the money could begin to flow out as fast as it's coming in right now. So it is a reasonable assumption to make that the markets will tank in the event of an FII exit, the rupee then will go the same way, and there will be that much less liquidity in the system.

While a combination of such events is usually enough to get the government into panic mode, the government would be well advised not to do the usual things in the event such a scenario does unfold. For one, with a Sensex price-earnings ratio of under 16 at the moment, the Sensex doesn't look terribly over-bought and so it is plausible that if an FII exit sees it dip below current levels, there will be other investors willing to step in. A fall in the value of the rupee, again, may not be a bad thing for the country's exporting community, especially

since most have been arguing that the rising rupee has hit their competitiveness. As for the resultant fall in liquidity which will occur once FIIs decide to exit and take their funds back home, commercial banks are sitting on excess liquidity (witness their SLR holdings vis-a-vis the statutory requirements) so it may not pose too much of a problem, even at a time when both the government and the private sector are upping their spending at the same time. In short, other than keeping a watchful eye, the government may not actually need to do anything.

Though the danger of a possible Tobin tax has receded after the RBI governor clarified his stand on the issue two months ago, there is another danger, that of the government not allowing a natural correction to happen. In order to preserve the feel-good factor, captive organisations such as the Life Insurance Corporation may be asked to step into the space vacated by the FIIs—in which case, the FIIs will find a good value for their shares even while exiting and LIC will be left carrying moderately over-priced stock. Though it is true that small investors do get hurt in the event of a market correction, getting LIC to step in would be foolish. For one, its ability to put in funds is unlikely to be able to match what the FIIs can take out. Second, and more important, a lot more people are at risk from an LIC which buys expensive stock as compared to those that take a hit if the Sensex tanks. The government would do well to keep that in mind and let the market correct itself.

Small savings, big problems

The National Small Savings Organisation (NSSO) operates a variety of schemes—the Public Provident Fund, the National Savings Scheme and others run through the post office network—which provide an important channel for long-term savings for individuals. The entire amount raised through these channels is passed on to states. The NSSO raises funds at a cost of roughly 8 per cent per annum and lends them to states at 9.5 per cent, the mark-up being justified by costs of collection. Each state is entitled to borrow from the pool to the extent of resources mobilised by it. In 2005-06, the Union Budget estimates net lending to states of Rs 87,000 crore; not a small amount by any means. But, given the interest rate scenario in the country today, 9.5 per cent looks like a rather high price to pay for funds and states are, therefore, reluctant to draw their entitlements. If this stand-off persists, the central government will have to service its obligations to savers without a corresponding flow of interest income from the states. This is clearly an untenable outcome and needs to be addressed at two levels. From a short-term perspective, the centre must ensure that it is at least able to cover its interest obligations to savers so that they do not turn into deficit-busters. In the long-term context, the distortions inherent in the scheme need to be addressed.

The immediate requirement clearly warrants a reconsideration of two parameters of the scheme.

Given current market conditions, when many states can apparently borrow in the 7-8 per cent range, it does not make a lot of sense to force 9.5 per cent borrowings down their throats. The Centre needs to significantly reduce the mark-up to a more realistic number. The other change required is to create a secondary market between states for the entitlements. If a state with a high entitlement feels it can get funds from the market at a lower rate, it should be free to lend what it does not want to other states for whom market borrowing is a relatively expensive (or unavailable) proposition. Both these measures should contribute to a larger appetite for these funds amongst states and thus allow the Centre to meet its obligations.

From a longer-term perspective, if states were to be subject to genuine market forces, most if not all would find it difficult to borrow at the rates being perceived today. Their access to low-cost funds is the result of various interventions, explicit and implicit, by the central government and the Reserve Bank of India. Rapid and dramatic fiscal reforms over the next couple of years will put a few states within reach of the market under their own steam. In a genuine market environment, a reasonable mark-up over 8 per cent may still be the most economical source of borrowing for states. If they want to find better deals, they will have to re-vamp their finances first.

We may have to wait till July for the next Harry Potter—or, if you prefer more High Literary fare, till September for Salman Rushdie's *Shalimar the Clown* to come out. But as the first section of this summer reading round-up should demonstrate, there's more than enough for armchair enthusiasts. Next week, we'll take a look at non-fiction.

Never Let Me Go: Kazuo Ishiguro (Faber) SF fans might be less than overwhelmed by the premise of the plot, pointing out that Larry Niven, William Gibson and our very own Manjula Padmanabhan have all dealt with the implications of clones and organ harvesting. But only Ishiguro could take a classic SF premise, transfer it to the environs of an English country house, and delve deeply into the internal, psychological life of clones. And few writers today have his talent for creating truly haunting, unforgettable fictional moments. The oddest piece of Ishiguro trivia ever discovered had to do with his "author trading card", like baseball trading cards, where he is apparently doing as well as Marianne Faithfull and better than Rick Moody.

Saturday: Ian McEwan (Jonathan Cape) The most famous examples of life-in-the-day novels are probably James Joyce's *Ulysses* and Virginia Woolf's *Mrs Dalloway*, so the bar's already set way high, not that

McEwan was daunted. The usual adjectives employed to describe a McEwan novel are "dark" and "menacing", often used in conjunction with lighter terms: ie, "darkly lyrical", "menacing but illuminating". Feel free to mix and match. McEwan's neurosurgeon protagonist has the perfect life, until he bumps into a violent, inarticulate thug on his way to a squash lesson. This random encounter brings darkness into his house the same evening. McEwan pits peace rallies against 9/11 and Iraq, poetry against knuckledusters, to mixed effect. *Saturday* resembles Coetzee's *Elizabeth Costello* in its preoccupation with polemics and digressive arguments, but is faster paced and more coherent in its plot. Definitely a Booker short-list contender, despite the reviewer who was so less than grunted by *Saturday* that she echoed Dorothy Parker's sentiments about certain books not to be put down lightly, but to be thrown with great force.

Conversations in Bolzano: Sandor Marai (Viking) Sandor Marai used to be Hungary's best-kept secret—like goulash, but more palatable. Born in 1900, he sur-

THE CHINESE ECONOMIC MIRACLE - III

The hare and the tortoise

If India completes its second generation of reforms on time, it could overtake China, says Deepak Lal

What are the lessons from the Chinese economic miracle for India? Who is likely to win the race for economic growth—the hare or the tortoise? These are the questions I take up in this column. I have maintained (see Chapter 3 of my *Unfinished Business*) that there are greater similarities rather than differences in the policies followed and their outcomes in both the periods of economic repression and reform in India and China. China carried its repression further as it has its reforms than India. But in both countries the liberalisation of foreign trade and the ending of planning gave a boost to growth. The major difference has been in their respective investment rates, with China's at over 40 per cent of gross domestic product (GDP) being roughly twice that of India's. But, given the continuing deadweight of the SOE leg on the Chinese growth path, this has not led to a commensurate difference in their growth rates during their reform periods, with Chinese growth between 1978 and 1998 being 9.7 per cent per annum on official and over 7 per cent per annum on the best independent estimates, whilst India grew by 6.1 per cent per annum from 1991-2000 (see table).

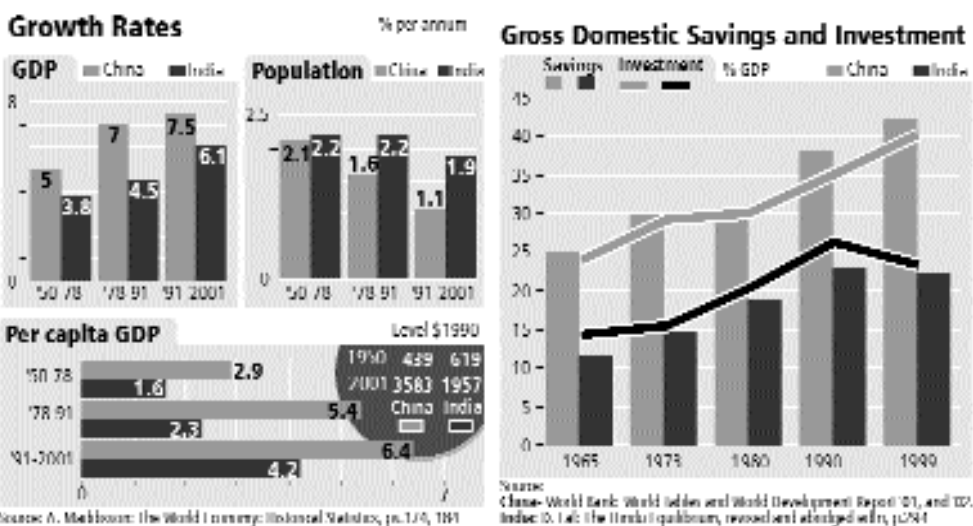
But the growth in China has been more labour-intensive than India's. This was the unintended consequence of the end of collectivisation in agriculture which led to an explosion of labour-intensive small-scale rural industry for export. This export led industrialisation was facilitated by the much better and more extensive infrastructure created in China, and by the freedom to hire and fire as well as the absence of any 'social' burdens carried by firms in this fast growing non-state sector. India by contrast continues to hobble the development of small-scale and labour-intensive industry with its policy of reservations, and refusal to repeal the archaic labour laws it inherited from the Raj.

In both China and India the dynamics of their growth have been provided by areas which the State

had overlooked as being of little importance: the small-scale rural industries in China, and the information based service sector in India. These were the areas where capitalism was allowed to take its natural course and once foreign markets were opened with the liberalisation of foreign trade, the native wit and entrepreneurship of the economic agents not subject to the dead hand of the State, generated a dynamism which no planner could have created. Unlike the Indian, the Chinese policy elite has fully embraced capitalism. The new (often Western trained) mandarins who run the Chinese state recognise, as many in India still do not, that this is the only route to both prosperity and power for their nation—and like mandarins of yore, it is the Chinese State and not any ideology that they serve. They are desperately seeking ways to remove the remaining vestiges of their dirigiste past: the loss making state enterprises. India by contrast seems stuck with its 'Left' still unwilling to abandon its past dirigisme, who continue to block the necessary privatisation of its public enterprises.

These differences in the embrace of global capitalism are reflected in both the much greater trade liberalisation undertaken by China and its more relaxed attitudes to foreign investment. Thus whereas exports were 19 per cent of Chinese GDP in 1998, they were about 8 per cent in India. Whilst the stock of foreign direct investment (FDI) was \$261 billion in China in 1998, it was a mere \$13 billion in India. Moreover, the foreign investment in China which has flowed to the non-state sector from the Chinese diaspora to finance industrial exports has loosened the constraint on its growth from its weak domestic capital markets. The multinationals, by contrast, have been lured into joint ventures with state enterprises to service the large domestic market and have usually lost their shirts (see Tim Crissold's account in *Mr. China*, and Y Huang: *Selling China*).

In both countries wherever growth has occurred there have



been dramatic reductions in poverty. However whilst labour intensive industrial growth seems to be spreading faster to the hinterland in China through fierce locational competition for joint ventures with foreign investors, the Hindu heartland in the eastern Gangetic plain still remains mired in its ancient equilibrium. While inequality had increased in China since the planned period, there is no clamour in an ostensibly Communist country for egalitarianism. This is because like India, China for millennia has been a hierarchical society. It was the foreign Enlightenment virus of socialism which for half a century infected their intelligentsia, but whereas the Chinese seem to have overcome it, India's intellectuals unfortunately still remain deeply infected.

From this it would seem that there is no contest in the growth race between the hare and the tortoise. But there are some signs that appearances may be deceptive. In my last column I had discussed the fragility of the Chinese financial system. Though India's financial system is healthier, it shares with China the problem of unsustainable fiscal deficits fuelled by economically unjustifiable subsidies. As I have suggested, China might be able to tackle this problem more easily if it used its foreign exchange reserves creatively. By contrast, the

political roadblocks to ending the subsidies debauching the Indian budget remain significant. Nevertheless, India currently has a head start in both the instruments it can provide for savings as well as in the mechanisms through the financial system for their efficient deployment.

There are two other advantages which India has over China as part of the legacy of the Raj: the rule of law, and the English language. Even though China has in the most recent revision of its Constitution put private firms on an equal footing as state owned firms, entrepreneurs are still suspicious of the State. When Forbes recently published a list of the top 50 Chinese millionaires, the individuals complained, as the tax authorities showed an interest. It explains why most of these new entrepreneurs rely on self or foreign financing of their firms and are reluctant to put their head above the parapet by listing their companies on the stock exchange. This cannot bode well for the future of Chinese growth.

India's advantage in having a large pool of English speaking people is likely to be eroded in a generation. Apart from the much higher literacy rate in China, it has now decreed that everyone from the age of five will have to learn English—the commercial and scientific lingua franca of the world. Given its fierce-

ly meritocratic education system, without any quotas or affirmative action, it is on the way to producing one of the most highly skilled populations in the world. This is a danger India needs to guard against, by helping the spread of private schools in the rural areas and abandoning the Mandalism which has already done great harm to its system of university education.

If affirmative action is extended to the private sector, it would further handicap India in its ongoing race with China.

Last, but not least, whilst China with the ageing of its population is likely to see an end to the savings bonanza promoted by the demographic transition accompanying its one child policy, when the dependency ratio declines as the birth rate and population growth rate fall, India is just entering its own demographic transition. These life cycle effects will raise Indian savings for the next few decades. This should allow a substantial rise in India's investment rate, just as after 2010 demographic effects lead to falling Chinese savings rates. If by then India has completed the second generation of reforms, built up its infrastructure and fully integrated itself into the world economy, we might find that the tortoise overtakes the hare. This race between the two Asian giants is set to be the most dramatic event of this century.

A pervasive workplace misery

MICHAEL SKAPINKER

My daughter wants to be a journalist. Do you think it's a good idea?" a taxi driver once asked as he drove me back to the *Financial Times*. "Well," I said, "I love my job." My driver gave an astonished snort. "I love my job. Do you know how few people can sit at the back and say that?"

Fewer than ever, according to The Conference Board, the business policy organisation, which last week reported a substantial decline in employee happiness. Only half of Americans were satisfied with their jobs, down from almost 60 per cent in 1995. Only 14 per cent of today's employees said they were "very satisfied" with their work. One-quarter said they were simply "showing up to collect a paycheck".

It made little difference how much employees earned or how old they were. Those earning more than \$50,000 (£26,000) a year were a little happier than those earning less than \$15,000, but not much. Nor was discontent confined to the PlayStation generation. The sharpest decline in workplace happiness was among workers aged 35 to 44, with the second biggest fall among the 45 to 54 year-olds.

Forty per cent of employees felt disconnected from their employers and two-thirds said they did not identify with their employers' business goals.

Watson Wyatt, the consultancy said its own survey showed that only 51 per cent of US employees had trust and confidence in their companies' leaders. In the UK, fewer than one-third had any confidence in their company leaders.

You can have some fun with these statistics. But we do not need surveys to verify the evidence of our woe and ears. A visit to a hotel or a call to a call centre on either side of the Atlantic will confirm that workers are grumpier than they were a decade ago and customer service worse. Why are workers so miserable? The Conference Board and Watson Wyatt offered several explanations—corporate scandals, poor communications and outsourcing among them. But none of these stacks up. Corporate scandals affected a handful of companies. Very few business leaders are criminally corrupt and their employees know that. Poor corporate communication is nothing new; indeed, companies probably tell their staff more than ever.

Outsourcing is a likelier explanation, but it is only part of the story. The majority of workers are unaffected by outsourcing. Most people hold on to their jobs for as long as they ever did. The idea that work has become transient and that companies have slimmed to a core of permanent jobs and outsourced the rest is a myth.

In both the UK and the US, there has been some decrease in male job

tenure and an increase in how long women stay with one company. However, the Chartered Institute for Personnel Development says average UK job tenure has remained stable for the past 30 years. The US Bureau of Labor Statistics says that there has been little, if any, decline in job stability in the past 20 years. The bureau reported last year that half of the employees aged 45 and over had been with the same company for more than 10 years.

Investors do put their money at risk, but today's shareholders are big institutions that can spread their risk. Employees on the other hand, rarely earn enough to make substantial savings

What outsourcing has done is add to the insecurity of those employees who remain in their jobs. It has also contributed to employees' sense that they have become a business's principal risk-takers.

In start-up company, it is clear who assumes the risk: the entrepreneur who often has to offer the family home as security for the new enterprise's debts. As companies grow, however, and a new generation of managers rises through the ranks, risk rapidly shifts away from the executive suite.

Top executives certainly put their reputations at risk. Dismissal is public and distressing; witness

Carly Fiorina and Harry Stonecipher's recent departures. But huge pay-offs, share options and other perks mean sacked senior executives need never work again. They run no financial risk.

Investors do put their money at risk, but today's shareholders are largely big institutions that can spread their risk by investing widely. Employees, on the other hand, rarely earn enough to make substantial savings. In the past, their

future was secured through a defined-benefit pension plan, guaranteed by the employer. Those plans, however, are being replaced by riskier defined-contribution schemes. Usually, those asked to assume a greater risk demand a premium. Employees pushed into less secure pension plans should be insisting on higher salaries to compensate. Some are, but many are in a weak position. This is where outsourcing matters. Even if your job is not outsourced, there is always the threat that it could be. Whether you assemble a car or compile the accounts, someone, somewhere is

ready to do the job for a fraction of your salary.

Employees' unhappiness should worry companies. How would they respond if they discovered half their factory equipment was malfunctioning? Some companies may try to do something about employee discontent, but most will shrug it off. The financial cost of restoring staff security is high and the cost of unhappiness is rarely quantified. This is a gloomy conclusion for grumpy employees, so here is a joke to cheer them up. A human resources executive dies. She arrives at the Pearly Gates, where she hears that her case is so finely balanced that she can choose between heaven and hell.

She is shown around hell by the devil himself. Her old colleagues are all there. They hug her, invite her for a round of golf on a perfectly manicured course and treat her to a lobster dinner. The next day she is shown around heaven. It is perfectly pleasant, with clouds, harps and the rest, but with none of her old pals. She chooses hell. She walks back through its gates to a completely different scene: it is strewn with rubbish, a cold wind is blowing and her friends are dressed in rags. "I don't understand. This isn't what I saw yesterday," she tells the devil. "Ah," the devil replies. "Yesterday we were recruiting you. Today you're staff."

Financial Times

Summer reading: Fiction



vived World War II but had to flee the country for first Italy and then the United States, where he committed suicide in 1989. The first of his books to be translated was *Embers*, where two men talked at interminable but very lyrical length over the course of a night about such matters as friendship and rivalry and masculine pride. For *Conversations in Bolzano*, Marai chose Casanova as his protagonist, facing off with the Duke of Parma for the love of a woman. All three of them talk at interminable but lyrical length, over the course of several nights, about such matters as passion and the death of love. You know what to expect; the story is dated since 1940; but Marai takes you back to a time when long interrogations into the meaning

of life were still the stuff of great, spellbinding literature.

The Shadow of the Wind: Carlos Ruiz Zafon (W&N) A long-forgotten book by a long-forgotten author is rediscovered by a young boy growing into manhood in Barcelona; but someone wants the author's name, reputation and books to disappear into oblivion. Zafon came up with a brilliant idea in the form of the "cemetery of forgotten books", a place where every book has at least a chance of discovering a reader. As to the rest, he introduces skulduggery, romance, and twists in the tale every few pages to form a baroque, bizarre romance. The author is a screenwriter based in Los Angeles, and drew some complaints from residents of Barcelona who griped that it's always raining or cold in the city as depicted in his book. Still, a great read, especially for bibliophiles.

The Alchemy of Desire: Tarun Tejpal (HarperCollins) Rarely has a simple blurb caused so much heartburning in Delhi's literary circles. But then this one—"At last—a new and brilliantly original novel from India"—was handed out by V S Naipaul,

known to bury debut authors rather than praise them. Tejpal accompanied him to Stockholm when the Great Curmudgeon won his Nobel, though, and the friendship between them is of long standing. The book's about a young couple's odyssey into desire and marriage, with the point of fading lust marked by the narrator's growing obsession with a ghost from the past, in a very literal sense. I normally resist coupling book titles, but not very hard. Think *Love Story* meets *Plain Tales from the Hills*. Among the crop of other fiction releases, some titles need special mention. Keep an eye out for Suketu Mehta's fiction debut, Siddhartha Deb's second novel and for Anjali Bannerji's first novel for adults; rumour also has it that Kiran Desai is working on a second novel that is a considerable departure from *Hulabaloo in the Guava Orchard*. More young adult fiction, children's fiction, chicklit and Diaspora Lite are inevitable too. Kunzang Choden's *The Circle of Karma* (Zubaan/Penguin) is billed as the first novel by a woman from Bhutan. It follows the journey, first literal and then increasingly spiritual, of 15-

year-old Tsomo as she attempts to answer the question: "Where can I travel?" Anjali Bannerji's *Maya Running* (Penguin) is a neat twist on the standard children's tale of growing up, dealing with school, first love and identity issues; she writes like a Judy Blume acolyte and finds unusual solutions to Maya's dilemmas about being an Indian in Canada. Not at all preachy, which is rare when you consider most Indian books for children.

KP Singh's *The Road to Raisina* (HarperCollins) is a light but thoroughly enjoyable read for denizens of Lutyen's Delhi. Singh's formula is pure Jeffrey Archer with a dollop of desighee: take three schoolmates, throw them into the maelstrom of Indian politics, and have them fight it out for the PM's chair. The plot has a few loose ends and holes, but these will be papered over by the dry sound of bureaucrats and ministers chuckling. And Rupa Gulab's *Girl Alone* (Penguin, the one with the brand endorsement from Shobhaa De) is a reasonably entertaining and astute entry into the Indian chicklit world. Her heroine is a cough syrup addict who can't quite find her man; she's also the face of the new single Indian woman, to put it in tabloid terms. Gulab's style is brisk, pretty funny, and not unlike what's been coming up on blogs like Bridal Beer of late.

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