THE FINANCIAL EXPRESS
www.financialexpress.com

Fuelling a balance

Handle differential tax on diesel & petrol cars carefully

Between them, petrol and high-speed diesel account for over 46% of the central government's total excise duty collections as per the figures from the Comptroller and Auditor General. One would expect that as petrol or motor spirit is taxed at a specific duty of ₹14.35, plus suffers an additional excise duty of 2% and is the preferred fuel for cars, the receipts from it would be far more than from diesel. This would be despite the larger usage of diesel as it is taxed at only ₹2 and is priced cheaper. But successive CAG data shows that the receipts from the two are now almost equal at 24% and 22.5%. Diesel has closed the gap with petrol because of its enormous lower duty advantage and the government's obstinate refusal to free its pricing, because of which the differential with petrol has become enormous. This is at the root of the absurd situation which is developing in India where diesel-powered cars have replaced petrol-driven cars as a mass choice. As the *FE* story of Tuesday shows, the pace of diesel consumption by automobiles has now begun to outpace petrol. The impact of this development is on the carbon footprint of India. Improvements being made in other sectors will be negated by this trend. In this context, the petroleum ministry's plan to even out the prices of petrol and diesel—and asking the finance ministry to make diesel-powered cars costlier—makes sense.

This would mean the finance ministry will have to balance a lower excise duty from petrol, whose demand is relatively inelastic, with the rising collection from motor vehicles. Of the top ten categories that account for 80% of the total excise duty collection, motor vehicles come in at the seventh position, with a share in excise duty of close to 4%. Any comparable tax will have to be very heavy on automobiles to keep the finance ministry solvent in a year when collections from all taxes are heavily down. To do so could quickly become a ham-handed approach that will ruin India's position as a destination of choice for international auto giants. At the moment, India is a very attractive proposition for these companies, and an unreasonably high tax on diesel-powered cars could very well sour their interest. The stakes riding on these investments are high too, and a differential tax on petrol- and diesel-driven cars will impact the proposed international investments in diesel cars. Imposing tougher standards of emission is a far better idea at this juncture.

Takeout expressway

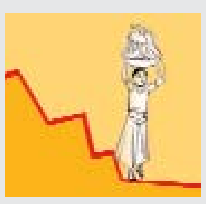
IIFCL changes rules in favour of speed & transparency

More than one and a half years after the takeout financing scheme was announced by the government, its details are still being worked out. The total offtake is just about ₹2,200 crore, to leverage an investment requirement of ₹50 lakh crore ($1tn) within five years. Takeout financing, which basically means removing a project from the balance sheet of a bank by a long-term financing institution, still needs to iron out glitches before it takes off. India Infrastructure Finance Company Ltd (IIFCL) has not moved with the alacrity needed to make this infrastructure financing plan attractive. Part of the problem lies with the constitution of IIFCL, which is still a committee-driven organisation instead of a board-driven one, which means members could have conflicting interests. The other is the conservative stand of RBI. For RBI, safeguarding banks' interests comes before allowing them to finance potentially destabilising projects like infrastructure ones, beyond a limit. This means IIFCL has a limited menu to choose from to offer takeout financing. Having successfully navigated a project through the more difficult construction phase, banks would be keen to retain them on their books and earn interest rather than sell them to IIFCL. Change in rules by IIFCL on Monday will take care of some of these problems. For instance, it will now offer a takeout fee of 0.3% of the loan amount as compensation to banks.

For projects, the pricing mechanism of takeout finance will be based on the credit rating of infrastructure projects, which means similarly positioned projects will be priced the same instead of being subject to negotiations with developers. Transparent pricing means viable projects will get funding at an interest rate linked to the benchmark lending rate of IIFCL. Also, while under the existing norms takeout financing can only be done one year after the scheduled commercial operation date of the project, this rule has been slackened. For road projects, takeout finance can now be offered any time after the commercial operation date and this has been relaxed to six months for projects in other sectors. These changes, including the option to project developers to directly approach the company, will put pressure on the banks to rejig their portfolios. To what extent banks move to the new beat is worth watching.

POSTER GIRL

Child labour is declining in India. We have many factors to thank for this



WHAT the latest NSSO data shows is that in 2009-10 there were 4.9 million children employed as workers, down from around 9 million in 2004-05, a decline of 45%. But there will be no single stand-out reason for this welcome decline of child labour in India. A combination of policies that distribute the growth dividend and a rising skills requirement across sectors is cutting down this relic of poverty. MGNREGA, for instance, has seen more people getting employed (according to data on the MGNREGA website, the scheme provided 283 crore person-days of work in 2009-10), which goes a long way in reducing the economic pressures on households, one of the key driving forces for child labour. A related trend is that fewer women are joining the workforce. Between 2004-05 and 2009-10, the labour participation rate of women fell from 22% to 18%. A likely explanation for this is that with more girls going to school, fewer are available in the labour force—around 12 million more girls enrolled in schools between 2004-05 and 2009-10. The education of women has multiplier effects by way of a positive impact on children's health and other wellness indicators. The same should hold in terms of education as well—an educated woman is less likely to send her child to work than send him to school.

Importantly, the right to education Act, which institutionalises free and compulsory education for children between the ages of 6-14, would also have reduced the number of children in the workforce. Finally, the rise in the technical requirement of labour in sectors even such as construction has made it loss-making to employ children. This is evident from anecdotal evidence too. In total, this is great news for Indian children and also for the Indian government, for this provides added reassurance that its social welfare schemes are indeed working.

Dragon's not got a straw house

Far from being an overbuilt bubble, real estate is a real engine of growth in China

For some time now, newspapers and the blogosphere have been full of reports of "ghost towns" in China—immense buildings, seemingly empty. The most notorious is Ordos in Inner Mongolia province. Many have been quick to conclude that the property sector in China is an overbuilt bubble. That's simply not true. Property is a key sector in the economy and is a legitimate investment for many people.

China built 1.6 billion square metres of residential floor space last year. After China began dismantling state-supported housing in the 1990s, the property sector has transformed into a vibrant private enterprise.

DILIP PARAMESWARAN

Rising urbanisation has created a need for a continuous supply of housing. For the first time in the country's history, more people lived in urban areas than elsewhere in 2010, following a steady migration of labour to urban areas.

Housing has also become an important store of wealth for many ordinary Chinese. Faced with negative real interest rates on their deposits, people have turned to housing as one of the few viable avenues for deploying their savings.

For the local governments too, revenues from land sales (a misnomer, since they are really revenues from leasing land) have become an important source, generating over 40% of their cash flow.

Given the sector's importance, the government has been regulating it closely. In 2006-07, the government implemented a series of interest rate increases, higher down-payment requirements, and stricter land sales policies. Following the global financial crisis, the policies were relaxed and the economy was pumped up with fiscal and credit infusions to stoke economic growth.

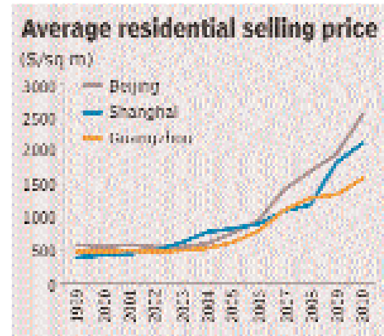
But when the property prices rose again in 2010, the government imposed a fresh set of policies, which included residency requirements and limited the number of properties that each resident could buy.

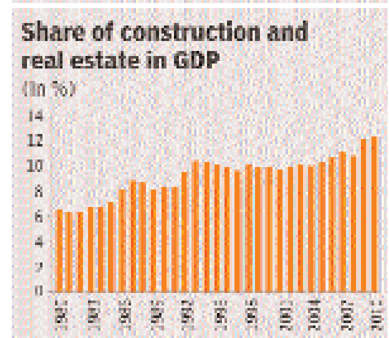
The policies have arrested the whole sector in its tracks. Prices have started sliding with 35 of 70 cities reporting a price drop in October from the previous month.

Developers have been affected not only by stalling sales and rising inventories, but also by restricted availability of construction credit. The larger ones have been able to raise finances from overseas US dollar bonds, but many smaller developers are under greater distress. Unlike in 2007-08, when the developers were caught short of liquidity, many of the larger developers have been able to read the policy direction better this time and have saved cash and have curtailed land purchases in preparation for a "long winter".

Ironically, local governments have been among the most affected. Their land sales have plunged, affecting the infrastructure projects on which their growth depends. This year so far, the top four cities (Beijing, Shanghai, Shenzhen and Guangzhou) have seen their land revenue fall by 30%, while the next 15 cities have seen a fall of 26%.

Any policy relaxation would depend on a few factors. One is inflation. As inflation declines, the country will be able to loosen monetary policies as well as the supply of bank credit (which is subject to a hard numerical ceiling every year). This has already started with a cut in bank reserve ratio by 50 basis points after inflation declined to 4.2% for November from 6.5% in July. The second is the property market itself. If the sector gets into more distress, it could spark dissatisfaction among existing property owners, most of whom are middle-class; it would also strain local government finances further. The third is the upcoming change in leadership in China next October, when the current President and Premier will give way to the next set of leaders. Until then, the government may not wish to relax its control on the property sector. My personal expectation is for some loosening towards the end of the first quarter or in the second quarter of next year.





Source: National Bureau of Statistics

The Chinese property sector differs from the Indian in many ways. In China, land is owned by the state and is only given to the developers for specified use for a period of time, whereas land is privately owned in India. Finding large-size land is easier in China. One of the projects I visited near Guangzhou was a mammoth 6 million square metres of site area. The scale of individual developments in China is often much larger, as is the size of the developers. For instance, the land bank of Evergrande, one of the largest developers, is 135 million square metres and its annual sales volume is 12 million square metres. Although developers are not allowed to borrow directly, they have set up offshore holding vehicles, listed in Hong Kong, which borrow in the offshore bond markets and inject the funds into China as equity. This creates an important additional source of financing for them.

Safeguards for buyers include the restriction that a developer cannot launch pre-sales of projects until a certain percentage, usually 65-70%, has been completed. Developers are also required to open escrow accounts with banks and use the funds from pre-sales only for completion of the same project. Although these rules vary to some extent from city to city, and may not be enforced strictly, they still offer some comfort to the buyers.

A well-developed property sector is an essential component of growth. It is best that India, too, accepts the need for urbanisation and a successful property sector.

The author is credit strategist, Macquarie Asian Markets in Singapore. He is not a member of the research department. These are his personal views

Reorganise states, but for right reasons

To begin with, let the Planning Commission come up with a better grip on rural migration

On the important issue of smaller states, there are arguments for geographical reorganisation to improve well-being. But the issue is being raised in a bizarre manner, which can only harm the polity. Serious arguments for reorganisation of states can be traced back to the well-known Panikkar Commission. At the conceptual level, the major advances were made in the 1980s. It was then that two powerful principles were enunciated. The first was to decentralise effective governance power through the Panchayati Raj principle. Regional political parties find that anathema, for it erodes their sectarian base and, in fact, raises empowerment and development issues, which they find difficult to handle. The second was the need to reorganise development along geographical resource lines called agro-climatic considerations. Land, water and climate was the base of poverty and exploitation, but the problématique could be turned around from a viscous to a benign circle. Local bodies supported by resource-enhancing policies could frontally attack rural backwardness and poverty. It was also perceived that cultural strengths were built around the soil of this great country. In the long run, that would be the base of political reorganisation moving away from the divisive games played to hang on to the crumbs of power.

In fact, these principles are becoming more urgent. Globalisation has not only meant an 8% annual growth but a great churning in which millions of people, including farmers, artisans and workers, are moving in search of higher incomes from small villages to large villages, and from there to small towns. Major political parties, our great globalisers and the Planning Commission have all missed this great movement. Rahul Gandhi had his finger on the pulse when he said that while travelling he learnt that millions of people are moving but nobody is bothered. Since it is the truth, and the neglect hurts the existing myopic leadership, instead of doing something about it, the reaction we get is to trash the legitimate comment on the system giving beggar wages—worse still to break up the problem so that our political backyard is intact. There is no earthly reason to break up the Indo-Gangetic Plain into Paschim, Awadh and Purva. The Purva has been exploited on account of the irresponsibility of the powers and, in fact, will link very well with the Paschim and the Awadh. The migration has not only happened to the metros but also to the Paschim, which has been ignored.

The chapter on rural transformation in the "Approach to the Twelfth Plan" begins by saying: "The Census of 2011 estimates that 833 million people continue to live in rural India." But until very recently, the Planning Commission was projecting that 870 million persons would live in rural India in 2011. They underestimated the rural population moving to small (Census, not official) towns by 37 million people.

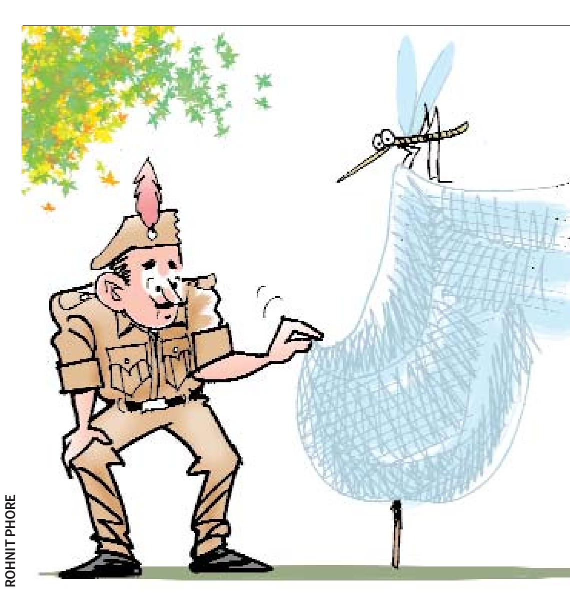
YOGINDER K ALAGH

That is a whopping number and, for an approach titled 'inclusive growth', a critical slip up. More perceptive leaders are catching up with this great movement.

Worse still, the Planning Commission, having missed the bus on decentralised urbanisation in the last decade, still continues with its old projections for the future. Rural population, it reiterates, will be 60% in 2030. This author in his columns since 2006 has been projecting that the rural population going to small towns and bigger ones is underestimated by 10%, by 2020 and for that matter 2025. The persons living in villages will go down to 58% in 2020 and 55% in 2025. This compares with the official projection of 68% in 2020 and 64% in 2025. We refer to the UN studies and several others to buttress our work. Now the facts are in for the country. Such serious mistakes in policies are made because of an inability to catch major societal trends.

For infrastructure, having missed the emerging markets, the Approach Paper is terribly weak: "Road connectivity, development of horticulture, dairying & other animal husbandry and expansion of cash crops, provide the necessary wherewithal for greater market access of the farm sector. This is particularly important for the segment of 'high value' agriculture, where the demand pressures are going to be most intense in the coming years, and major investments are needed in the development of efficient value chains to save on high wastages and intermediation costs. This is logically the domain of the private sector." For the run-of-the-mill politicians, the press and the planners to miss out on the fact that infrastructure for a diversifying agriculture is a planning task and even PPPs are difficult in small towns is sad. So, in spite of all the good words, there is no strategy for widespread agricultural growth. Instead, it is easy to shoot the postman when he says you are ignoring the poor migrating to towns. That way you don't have to build the infrastructure for the farmer in the Paschim and the Awadh. You can try and get more votes by dividing for a few more years. The resource and cultural base of political organisations and the efficiency requirements of administering land, water and social programmes, which were the core of the Panikkar Commission, are being ignored.

The author is a former Union minister



ROHNIT PHORE

EAVESDROPPER

Small mosquitoes, big deal

The impact of anti-corruption stir has become deeply ingrained in arms of the government. The NCC directorate has decided that nothing should come in the way of due diligence in ensuring honest tenders. It has therefore mandated that when the party with the best offer—L1—has to be rejected, the concerned officers cannot simply look at L2 or L3. They must expand their universe and search up to L21, not forgetting L25. Since the tender is for life-saving equipment for the para-military officers, it's worth the effort made, feels the directorate. The equipment in question is a mosquito net.

LETTERS TO THE EDITOR

A bumpy ride for IT giants

The recent opposition by the standing committee to shun the UIDAI project is another setback to progress. This experience will be a road-block for IT giants to take up any subsequent government project. The painstaking work by the UIDAI team, spearheaded by Nandan Nilekani, has not been taken in the right spirit and it would be shocking if the project suddenly comes to a halt. This would only dash the hopes of IT professionals planning to work on government projects in the future. The parliamentary committee has just voiced the opinion of critics without checking the facts and sifting the evidence properly. The world has been looking at the project with acclaim. The changing India needs an identity that can be used for multiple purposes.

Sunil Dutta, *Bangalore*

RNI Reg. No. 6188/61 ■ Printed for the proprietors, The Indian Express Limited, by Ms. Vaidehi Thakar at the Indian Express Press, Plot No. EL-208, TTC Industrial Area, Mahape, Navi Mumbai-400 710 and published from Express Towers, Nariman Point, Mumbai-400 021. Editorial & Administrative Offices: Express Towers, Nariman Point, Mumbai-400 021. Phone: 22022627/67440000. Fax: 022-22856323. (Air Surcharge: Rs. 10.00 Kolkata & Delhi; Re. 1.00 Goa & Indore)
Chairman of the Board: Viveck Goenka Group Editor-in-Chief: Shekhar Gupta Managing Editor: MK Venu Resident Editor (Mumbai): Shobhana Subramanian* (*Responsible for selection of news under the PRB Act)