Anglo-Saxon, not Asian, India?

Our affinity to the Anglo-Saxon countries is perhaps natural. English is the only "national" language understood all over the country, if only by a minority. Most of our opinion makers have studied in the English language and still seem to borrow more of their ideas from Chicago rather than Beijing, despite China being the most successful economy of the last 30 years, indeed in global economic history, in contrast to the financial excesses of the Anglo-Saxon banking industry which recently brought the world close to a global depression. Our parliamentary/democratic institutions, as well as the socialistic ideas in an earlier era, were borrowed from the British. To be sure, now-a-days we seem to be far more under the influence of American economic philosophy and ideas, particularly in relation to the financial and industrial economies.

Take the question of the industrial sector. Both the U.S. and U.K. have seen a very significant de-industrialisation of their economies, partly because of the huge trade deficits. I sometimes wonder whether we are falling into the same trap of considering a globally competitive manufacturing sector to be a peripheral issue. There are a few immediate provocations for this thought:

⇒ We seem to be completely unconcerned about the mounting merchandise trade deficit which has gone up from barely $ 15 bn in 2003-04, to $ 120 bn in 2009-10. Perhaps the easy financeability of the deficit through invisibles and capital flows leads to its benign neglect; in the process, we seem to forget that while exports, whether of goods or services, create domestic jobs, remittances are a reflection of the jobs created elsewhere and, to that extent, no reflection of our competitive strength.

⇒ Manufacturing employment in the Anglo-Saxon countries has fallen sharply in the last three decades; in our case it has been stagnant.

⇒ Another manifestation is the complete unconcern about the years and years of delays in acquiring land for major projects in several parts of the country. (To be sure, some states like Tamil Nadu and Gujarat are exceptions to this.)

The Anglo-Saxon influence is also manifest in the financial sector. Competitive strength requires organisation, innovation and investment, but the exchange rate can more than negate their contribution. Instead of learning from Beijing how to manage capital flows, coming on top of a huge current account surplus, even while managing the exchange rate in the interest of the competitiveness of the domestic economy, and keeping inflation under control, we seem to have swallowed the “virtues” of fully floating, market determined exchange rates, too often determined by financial flows than the needs of the competitiveness of domestic economy.

One wonders whether this approach is also extending to financial regulation. One recent example is the question of introduction of credit default swaps. A long report focusing on the procedures and regulations has recently been put on the RBI website. However, before such elaborate prescriptions are to be seriously considered, one would have liked a debate on how exactly the introduction of credit default swaps will benefit the real sector; how they are considered a superior instrument of credit risk protection on corporate bonds than, say, bank guarantees (which, incidentally, are banned by the central bank); why, assuming the answer to both the earlier issues being in favour of CDS, an OTC product is considered better than an exchange traded CDS contract, even when the underlying, namely corporate bonds, are to be traded on exchanges. (The G20 has called for moving all vanilla derivatives to exchanges). One would have liked such issues to be debated and analysed before going into procedures. Sadly, this is missing. Are CDSs “good” because that is how the Anglo-Saxon countries look at them, and seen as a major financial reform? By whom?

Some of the same questions can be raised about the recent release of the draft Comprehensive Guidelines on Foreign Exchange Derivatives. To be sure, they are an improvement over the earlier draft in some respects: dropping of the provision permitting the corporate sector to write “covered” options; dropping of leveraged zero-cost structured products; limiting use of cost reduction strategies and liability transformation to larger companies; etc. (To be sure, the assumption that they understand what they are doing is a large assumption in respect of too many of them.)

What one would have liked to see but is missing is a discussion of:

⇒ What lessons market markers and end-users need to learn from the spate of cases of losses by end-users in the Indian, and many other countries', markets;

⇒ A clear exposition of the purpose of the regulations (see, for example, the U.K Financial Services Authority's BIPRU document – each chapter of regulations starts with an articulation of its application, purpose, etc);

⇒ A discussion of the implications of exchange traded forex derivatives (currency futures and, shortly, options), to the OTC market etc.

The document also seems to ignore the supervisability of some of the regulations – the detailed procedures for "contracted exposures" for example!

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