

**Avalon
Perspectives
2020**



The Tipping Point

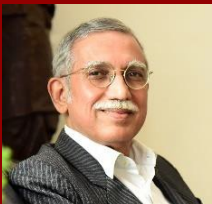
Part I

January 2020

- Raj Nair

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ABOUT THE AUTHOR



As a strategy consultant, Raj has helped companies across diverse industries in India, USA, Europe, and the Middle East to develop strategies, align strategy to vision, grow in competitive markets, restructure to make companies more customer focused etc.

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2020: The Tipping Point – Part I

By Mr. Raj Nair, Chairman, Avalon Consulting

2020 will be remembered for many years for the way things changed quite abruptly in India. That tipping point could be the annual Budget on Feb 1. Back in October 2019, I had written a note on this and presented it at the IMC Chamber of Commerce and Industry on November 25, 2019. I would urge you to read it by clicking on this link <http://www.consultavalon.com/insights/what-next-for-the-indian-economy>. Much of what has been predicted will happen, the rest may get delayed due to fiscal management compunctions.

The dire straits that the Indian economy finds itself in, was a long time in the making. From 2012 there have been a series of omissions and commissions attributable to many venerable institutions. The honourable Supreme Court of India passed judgements relating to telecoms, coal mining, iron ore mining, etc. with the intent to deliver justice by the letter of the law, but the collateral damage that it caused to the economy, investors, India's global reputation as an investment destination and the common man would make one wonder whether this was justice at all. The Reserve Bank of India with its hawkish interest rate policy to control inflation even when it was sub 3%, consistently remaining below its own exaggerated quarterly inflation forecasts, put paid to whatever growth the economy was struggling to achieve; that despite petitions pointing to the need to balance growth with inflation control. Successive Governments from 2012, have seriously contributed to sagging capital investments through poor policies, poor demand especially rural demand which was hit by two successive years of poor rains, non-payment of dues of businesses by government departments and public sector policies, and various other measures explained in my note. Unimaginative demonetisation destroyed supply chains and virtually crippled the informal sector of the economy which employs 93% of the labour force. It can be traced back to the naive belief that there were independent parallel black and white economies, and lack of understanding that cash changes colour between black and white several times in its journey. Cash is only a medium where the transactions could be legitimate or otherwise. IL&FS started a wave of problems for the NBFC sector leading to throttling of funds for consumer hard goods and SME businesses. Infrastructure and Real estate sector are now oversupplied and underfunded leading to NPAs affecting the whole banking sector. That leads me to the fourth set of players which contributed to the bad situation- many unscrupulous businessmen, who exploited loopholes to defraud financial institutions and the economy for their selfish gains. The Government's reaction to counter some of them, has been like burning a forest to kill a few mosquitoes but many of the mosquitoes are still flying, barring a Nirav Modi here and a Vijay Mallya there.

The cumulative effect of all this, has been that consumer buying power has fallen significantly. A supply side problem has now become a demand side problem. Ironically, the highly creditable move to implement GST, despite all its glitches, which will bring several long-term benefits by increasing efficiency and transparency, also causes short term pain. Efficiency and transparency also kill businesses that survive purely because of lack of these constraints to growth. e.g. with the travel time for trucking goods across the country having fallen due to GST, there are surplus trucks, closure of some associated businesses and lost jobs. In turn, the demand for new trucks has fallen at a time when the automobile sector is already struggling. Given the huge baggage of such businesses that thrive on inefficiency across sectors, and all the other problems described in the linked note, the situation harks back to the desperate times that preceded the great reforms orchestrated in 1991 by the then PM, Narasimha Rao.

The purpose of this communication is to explain what reforms to expect. They are explained in the link <http://www.consultavalon.com/insights/what-next-for-the-indian-economy>. The hypothesis for predicting these reforms is that they are essential but politicians in democracies postpone logical economic decisions till they reach a point when there is No Other Choice (NOC). The time for NOC has come. It is desirable that the Government creates more space for spends on growth drivers by temporarily moving off from the fiscal deficit glide path designed prudently for normal times. There will be an attempt to put more money in the hands of people. There is more than a reasonable chance that the four mother sectors (Automobile, Infra & Real Estate, Financial Institutions, and Textiles) that drive the economy, will witness significant reforms which are explained in the linked note. Narendra Modi desperately needs to taste success to leave behind a proud legacy. 2020 is the tipping point in his tumultuous second term. Since he matches the profile of a Theory X man (as described by Douglas McGregor in his seminal work), Modi can be expected to personally drive and control the reform agenda through his central team at the PMO, unlike Narasimha Rao who drove it from behind the scenes and orchestrated them through Manmohan Singh, who got the credit.

This merits so much attention that this year's new year note is in two parts, with the 'before the reforms' part being this note. The global economy is also up in the air in 2020, with Brexit happening in end January, the Phase 1 US-China Trade Accord and its negative implications on the struggling European economy, Trump's theatrics for his re-election after the move to have him impeached (which is not likely to succeed according to American experts), Iran- US dispute, planned elections in many countries including Iran, Taiwan, Ireland, the simmering clash of civilisations between Islam and the rest of the World, the emerging global fear of the Corona virus, etc. That will be covered in the next note in end February.

Our Values — The Avalon EDGE

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ENTREPRENEURSHIP

Enterprising ownership to transform ideas into pragmatic and profitable solutions

DEDICATION TO EXCELLENCE

Commitment to premier quality and highest standards in everything we do

GREAT VALUE CREATION

Focus on delivering maximum client impact through innovation and collaboration

ETHICAL APPROACH

Respect, fairness and transparency in all our interactions



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