THEIR VIEW

Navigating a world on fire: What the Kautilya conclave had to say

Discussions covered inclusive development, climate action and industrial policy quite well but fell short on our AI challenges

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PTI

Last weekend, the Institute of Economic Growth in partnership with the ministry of finance held the second Kautilya Economic Conclave. It brought together several current and former finance ministers, central bank governors and experts on different economic subjects from all over the world. Appropriately themed 'Navigating a world on fire,' reflecting the many burning global problems of the day and two ongoing wars, the conclave discussed different aspects of navigating this very challenging environment. I summarize below my takeaways on three subjects that struck me as being the most interesting.

The first is inclusive development: Homi Kharas provided evidence-based projections to argue that extreme poverty could be eliminated globally at a relatively low cost by providing unconditional one-time grants to those in extreme poverty as a core growth strategy. Indermit Singh Gill argued that from a growth strategy perspective, expenditure on infrastructure, education and health should be prioritized over income support grants. The floor discussion highlighted that political economy considerations are key for policy making. Income support and other grants are important for political leaders to nurse their constituencies today while benefits of expenditure on infrastructure, education and health will be realized only in the future. Hence, politically realistic spending patterns must balance allocations for short-term poverty alleviation measures like income support with investments in infrastructure, education, health, etc, for longer term benefits in a fiscally sustainable manner.

The second subject is dealing with climate change: Different aspects of it were discussed in several sessions. One key takeaway, which I have often mentioned in my *Mint* columns (eg: 26 April 2023) and elsewhere, is that technology is not the binding constraint in dealing with climate change. Global warming is already happening. But there has also been enormous progress in mitigation technologies. Commercially viable technologies for solar and wind power, green hydrogen, green steel, green mobility, carbon capture and sequestration, etc, are already being deployed. These will profoundly transform economies across the world from fossil-fuel based production systems to those based on renewable energy. However, this transformation will require investments on a massive scale. The resources required to finance this huge investment push, especially in emerging market and developing economies (EMDEs) in tropical geographies, is the binding constraint.

An estimated $5 trillion per year will have to be invested, including a transfer of about $1 trillion per year to EMDEs excluding China to supplement their domestic climate finance investments. Much of this can be privately financed, but private investments will not flow to EMDEs without adequate risk guarantees and insurance. The Independent Experts Group (IEG) on Multilateral Development Bank (MDB) reform, commissioned by the G20 at the instance of India, has recommended that MDBs should be repurposed to address global public goods, including climate change mitigation and adaptation. Tripling MDB operations to $390 billion by 2030 will enable them to provide the necessary risk guarantees and insurance. This will require far reaching reforms in MDB systems and procedures that the IEG has recommended.

The conclave discussions made clear that there is no conflict between climate finance and growth, since the huge investments required to contain and reverse global warming will also give growth a massive boost.

The third subject is lessons for India on industrial policy: Differing views notwithstanding, the discussions pointed to a core set of issues on which there appeared to be consensus. First, industrial policy should not be equated with trade policy and protectionist tariffs. Maintaining competitive exchange rates is a neutral means of switching expenditure from import substitution to export promotion. But border interventions like competitive exchange rates and membership of regional free trade arrangements by themselves may not help grow exports unless a supportive ecosystem is in place behind borders to raise productivity and lower costs domestically. This would include, *inter alia*, a world-class infrastructure and communications system in which India has taken great strides in recent years. But it also includes ease of doing business, in which India is lagging behind.

Industrial financing is another important part of the required ecosystem. Winding up term lending institutions has left a gap in long-term industrial financing which has to be filled. Skilling is also an important gap. Despite numerous schemes, the outcomes are disappointing. A large number of graduates, including technical graduates, remain unemployable because of the poor quality of their education. A related issue is investment in R&D. India's expenditure on R&D remains abysmal compared to advanced countries and EMDE competitors. Finally, the Productivity Linked Incentive scheme is a good initiative if its sunset clause can actually be enforced once enterprises reach the required scale. But picking winners can lead to regulatory distortions in Indian conditions. Small and medium size enterprises, which account for the bulk of industrial employment in India, have not been able to take much advantage of the scheme.

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The Kautilya conclave arrived at notable conclusions on inclusive growth, on which progress can be made through direct grants and long-term investments in health and education.

On climate change, it found no conflict between climate finance and growth, while the huddle also emphasized a need to differentiate between industrial policy and protectionism.

The conclave covered many subjects in addition to the three cited above. But the likely transformative impact of artificial intelligence (AI) was hardly discussed, barring a brief discussion by a co-panelist and me in our session. This was a disappointing omission, since in the next few decades AI is likely to have a profound impact on the way the world lives and works.

These are the author's personal views.

MINT CURATOR

America is no longer raising its children to be risk-takers

The over-supervision of kids is doing them more harm than good

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Risk-taking is a valuable skill that's often acquired early in life ISTOCKPHOTO

Like many people my age, I look back fondly on my free-range childhood. Now many of my generation have become neurotic helicopter parents—and their children are paying the price.

Over the last 60 years, in nearly every wealthy country (except France), the amount of time parents spend with their kids has steadily increased. And while parental engagement is better than parental neglect, this hyper-attention may be harming children.

A recent paper in the *Journal of Pediatrics* speculates that the increased anxiety and worsening mental health of children is correlated with more time spent with parents and less in unstructured, non-supervised play.

Historically, free play and time away from parents was an important part of childhood: It helped children develop independence, learn to handle conflict and disappointment, and also feel a sense of control over their environment.

Now women [in America] spend more time with their kids than they did in the 1960s—which is itself extraordinary, because far more women work today. Part of it can be explained by modern technology; household chores take less time than they used to. People also have more money and fewer children, allowing parents to lavish resources on their kids. And some of it is undoubtedly due to a more cut-throat economy and culture. Parents shuttle their kids to various activities and help them with their homework because they want them to get ahead of their peers.

The problem is that overbearing parenting robs children of a sense of well-being and prevents them from developing critical risk-taking skills. Children need to learn that success comes not from playing it safe and doing everything right, but from taking risks and bouncing back from failure.

This will be an important lesson for their future careers. People who take a risk to start a business tend to earn more. Even if they have a boss, people who take risks on the job (within reason) can advance more quickly. There are also career gains to be made from moving or just changing jobs. All of this requires comfort with uncertainty and ambiguity. And the benefits are more than just personal: America depends on smart risk-taking to fuel economic growth.

Yulia Chentsova Dutton, a cultural psychologist at Georgetown, has found that a child's "age of release"—that is, the age at which they are first allowed to go places alone or unsupervised—has an impact on their ability and willingness to take risks later on in life. She estimates that this age has increased by 6 or 7 years over the last few decades in the US, to between 12 and 14 years old. Dutton once asked her students how old they were before they were allowed to play alone, she tells me—and they laughed and said by the time they were allowed to be alone, they were too old to play.

Each new class, in Dutton's observation, seems more anxious and less able to assess and take risks. More and more students are afraid to take public transportation and some are reluctant even to leave campus. When she asks them to recall a hard or scary experience, they will mention things that would not have qualified a few decades ago, such as being approached on the street by a stranger.

To be sure, there are indeed some advantages to parents spending more time with their children. Partly as a result, childhood has never been safer in the US. And it's also important to point out that spending more time with the kids is not an option in many single-parent households, which tend to be lower-income. Still, when it comes to parents spending time with their kids, America may be past the point of diminishing returns.

Reversing this trend is hard. In a recent poll [conducted in the US], 84% of parents say their 9- to 11-year-old would benefit from doing more things on their own—but they find it hard to grant much independence. Only 33% of those same parents would let their child walk or bike to a friend's house alone, while just 50% would let them get an item in the grocery store while the parent is in another aisle. And, perhaps most sadly, only 15% would let their children trick-or-treat with other kids and no parents.

There is a great deal of social pressure for parents to be highly involved in their children's lives, and a great deal of shame if they are seen as neglecting their children. And in an arms race of enrichment, who wants to risk leaving their kids behind? This has it backwards: The best way for any parent to make sure their children aren't left behind is to teach them how to manage the risks they will need to take to get ahead.

GUEST VIEW

Online gaming taxation: Look for a practical way out

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India is one of the world's largest markets for online gaming, with thousands of jobs and millions of users. It got a boost during pandemic, attracted huge investments from venture capitalists and private equity firms, and has grown enormously. It has several startups and significant exports. However, these are challenging times for the sector. Its taxation slab as well as liability valuation mechanism were changed, and it faces a looming spectre of retrospective taxation—or call it tax arrears—that has seen it go from being a 'sunrise sector' to one whose survival is under a cloud. Many gaming companies are now in jeopardy, as they get notices of eye-popping GST demands, which some estimates place at up to ₹1.5 trillion, including penalties for late payment. In fact, the demand made of a single company is more than the total market size!

Let us briefly look at the background of the matter. In a post-Budget talk in 2022, the Prime Minister had emphasized the importance of online gaming, acknowledged its international market and said that India is exploring avenues to increase its footprint in the sector. Realizing the potential of gaming, the government has been forming regulatory mechanisms to facilitate its responsible and sustainable growth, commensurate with our socio-economic and cultural ethos, so as to take care of the problem of addiction, serve consumer interests and curb the proliferation of illegal offshore gambling sites. Union minister Rajeev Chandrasekhar has also asserted the importance of this burgeoning sector and the need of regulation for its sustainability and growth.

Since the implementation of GST in 2017, a landmark move designed to integrate and streamline indirect taxation in India, corporations have enhanced their compliance efforts and budgets to ensure strict adherence with it. This is reflected in impressive growth in GST collections month after month, for which the tax department must be unreservedly complimented, as also Indian businesses for compliance. GST processes, however, also involved the submission of numerous forms and reports through various online portals.

The gaming industry contends that ever since the advent of the GST regime, tax authorities didn't raise any objections or concerns when it filed returns with GST at a rate of 18%. On the other hand, the taxation authorities hold that they have an 'actionable claim' as the activity is covered under gambling, which would legally attract GST at 28% and not 18%, and so their demand for arrears is legitimate.

Therein, however, lies a fallacy. Prize winnings have already been disbursed to game players, leaving companies with only their already-taxed revenue. So the demands not only place an unjust burden on these operators, but also establishes a troubling precedent for other sectors. It introduces ambiguity into the business environment, which would ultimately hurt entrepreneurial spirits.

From a pragmatic perspective, the retrospective application of tax rules, even if it is based on a clarificatory interpretation, appears enmeshed in a legal and financial tangle. It has been argued that since the matter necessitated an amendment to our GST law by Parliament, it was more of a rule change than a clarification. Whatever it is, it can impact investor sentiment, and even revive memories of a retrospective amendment brought in to overturn the Vodafone judgement of the Supreme Court.

QUICK READ

What the tax authorities call arrears that they want gaming companies to pay has been challenged by the latter as another instance of unfair retrospective taxation.

It's a legal muddle but perhaps a resolution of this stand-off would lie in a compromise deal of the sort offered by the A.B. Vajpayee regime to telecom companies strapped for cash.

To recap, in the Vodafone-Hutchison case of retrospective taxation, in 2007 Vodafone had acquired Hutchison for $11 billion in a deal through an overseas holding company. India sent a tax notice to the UK telecom company. Vodafone challenged the notice in the Supreme Court, whose ruling favoured the company. The Union government amended the Finance Act and introduced retrospective taxation. In September 2020, a tribunal in The Hague ruled that India's retrospective tax bill on Vodafone breached an investment treaty between India and the Netherlands. It was subsequently reversed by the government to settle the matter.

The recent notices by Indian tax authorities raising humongous demands on online gaming industry based on a current interpretation of GST applicability pose a significant challenge to one of the country's fastest-emerging sectors. While the industry can still strategize and develop survival business plans to contend with the prospective application of GST on the full face value of deposits, a significantly increased burden, the barrage of notices sent to firms that aver they have been operating by the book could cause this revenue source to lose its promise.

The potential economic impact, legal uncertainties and business closures which may result from these demands of arrears could have several unintended implications. As the industry may not be in a position to pay such astronomical amounts, it may result in shutdowns or shift-outs, with offshore sites creeping in to fill a market vacuum, some of them illegal and posing security concerns. The government could consider taking a bold and pragmatic stance, as the Atal Behari Vajpayee regime once did with the telecom sector to grant it renewed capacity for expansion. Striking a balance between what is legally sound and economically doable would be crucial to ensure the continued growth and success of this burgeoning industry in India.