

South Asia

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India gives nod to foreign shops, at a price

By Kunal Kumar Kundu

The Indian parliament's approval late last week of foreign direct investment (FDI) in the multi-brand retail sector, and the run-up to that decision, turned what need not have been an event into a very notable affair.

Permission to allow FDI in the retail sector was not, in fact, a legislative decision but a mere executive decision and one that should have had an easy passage. But politicians being politicians - power hungry and in this case with an opposition smelling a weak ruling alliance - nothing is a given.

That meant that the entire ruckus over allowing FDI into India's US\$500 billion retail industry jangled already frayed nerves among working folk (whom these very politicians claim to serve): the common man and woman, who are trying to survive under high inflation, a slowing economy and an environment in which it is extremely tough to find a job.

The monsoon parliamentary session (which ended on September 7) was virtually washed away (I am referring to political and not heavenly intervention), what with the opposition, led by the Bharatiya Janata Party (BJP), using the issue of government corruption to prevent parliament from functioning after the Comptroller & Auditor General unearthed a scam with regard to the allotment of coal deposits for exploitation. Normal folk, though, were quite confused as the BJP itself has been mired in various controversies and corruption claims, with the most recent one involving the party president himself.

With a slowing economy hit hard by high inflation, a runaway deficit and faltering investment sentiment (aided and abetted by a slew of policy missteps that scared away foreign investors), credit rating agencies started to emphasize how vulnerable India was to a rating downgrade - from being barely investment grade to junk.

The UPA, led by the Congress party, made use of the intervening period before the present parliamentary session to announce a slew of measures that had all the appearance (at least to the rating agencies) of reforms, though real reform remains miles away.

The decisions to raise the diesel price by 5 rupees per liter (9.2 US cents, an increase that barely dents the huge oil subsidy) and allow FDI in retail (merely an executive decision) were not earth-shattering. However, given that these were likely to be controversial measures, the UPA seemingly went for them to divert attention away from the corruption issues plaguing the government.

However, with the UPA having been severely weakened politically, experiencing dismal results at various state level elections, the opposition smelt blood and tried to use this as an opportunity to make the government fall. So they insisted on having a debate on the feasibility of FDI, followed by a vote.

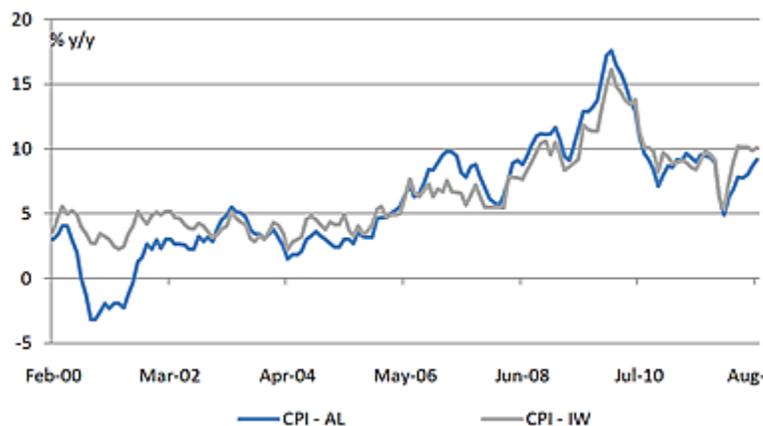
In the event, the entire debate was on anything but FDI, its one questionable merit being that the intriguing reality of regional politics was put on full view. Mamata Banerjee, the whimsical leader of the Trinamool Congress (a former member of the ruling alliance), wanted to bring a no-confidence motion against the government; yet there is no love lost between the TMC and various other opposition parties, and with highly inadequate numbers on the floor the effort proved duly embarrassing.

The opposition, in effect, failed to show a united face as some were ready to fight a general election with immediate effect while others were not prepared to take on the challenge with the same immediacy.

The actual debate was mostly ridiculously illogical, as those who wanted to have election sooner rather than later raised the specter of colonialism. They equated the international retail brands such as Walmart and Carrefour with devils that are out to create havoc to the economy, to the common people, and most notably to traders.

Little did it matter that existing and well-entrenched big domestic retailers have hardly had any impact on local traders; that individual states have every right not to allow foreign retailers in their territory; that locational clauses and back-end investment requirements are onerous; that if finally the parasitic middlemen are done away with then it is only the consumers who will benefit; while introduction of FDI in the retail sector could possibly also help bring down food inflation.

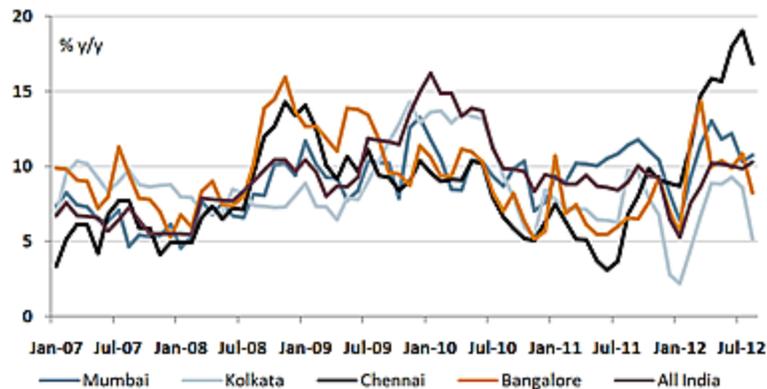
On the other hand, the government's claims for FDI in retail also do not really stand up to much scrutiny. India's high food inflation is a mostly a structural problem rather than being simply due to the existence of middlemen.



AL - Agricultural Labor. IW - Industrial Worker
Source: Government of India, author's calculation

As the chart above shows, rural inflation started to trend upward from 2006 onward and has since then generally remained above urban levels or at par. This coincides with two major decisions by the ruling government in 2006 - implementation of the "Mahatma Gandhi National Rural Employment Guarantee Act" (a job-guaranteed scheme that the government believes brought them back to power in 2009), and a massive spurt in the minimum support price for farm products from 2006 onward. Of late, the trend has been reversed but that is mostly because of the impact of drought-like conditions on rural income.

Also, the mere presence of organized retailing does not ensure lower inflation.



Source: Government of India, author's calculation

The fact is, domestic retailers have failed to build up necessary infrastructure, apart from setting up a few collection centers. Not surprisingly, Consumer Price Index inflation in metro cities (which are the predominant hunting grounds of domestic large retailers) continues to run well above the all-India urban average.

That apart, the restrictive location clause on retail FDI (outlets can be located only in cities with a population of more than 1 million), the substantial investment requirement for creation of back-end infrastructure and other factors will further limit the possibilities for foreign encroachment on the retail sector.

Clearly the entire debate about FDI was mostly based on wrong and hypothetical claims by both sides (scare-mongering by the opposition with respect to loss of jobs and business opportunities, and hypothetical benefits put forward by the government).

However, with every political party on its own, the government, with a bit of luck and loads of machinations, finally managed to get FDI in the retail sector underway by getting a mandate in its favor both in the lower house (where the numbers were mostly in the the government's favor) and in upper house (where the numbers were not).

While the debate has ended, one is not very sure about how much FDI will actually flow in to India - but the country is all the poorer for it because valuable policy-making time has been wasted, which the country can ill-afford.

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