Crony Capitalism in the Age of State Capture

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It is a controversy that is unlikely to go away. Arvind Kejriwal's salvo in the form of an FIR against Reliance Industries Chairman, Mukesh Ambani, Petroleum Minister Veerappa Moily and sundry policy makers against the decision to double the price of natural gas in India to $8.4 per million British thermal units as of April 1 has revived a controversy that the UPA government hoped had died. There is no doubting that Reliance would be a major beneficiary of the decision. And that at a time when it is being accused of having inflated capital costs to garner a larger share of profits (as compared to the government) from the K6-D6 fields leased to it and of having failed to ensure gas output levels and therefore shareable revenues promised in the original revenue sharing contract. The loser has been the government.

With the election barely weeks away, the controversy could snowball. But some like Veerappa Moily who are seen as behind the decision with support from "above" seem convinced that they can brazen it out and deliver a policy the damage of which will have to be addressed by the next government. That damage could include huge losses in the power and fertiliser sectors and reduced access to power to consumers due to both high prices and supply shortfalls. Benefitting Reliance seems to be a priority, to which all else is being subordinated. Some say this is crony capitalism, where a state (and not market) determined price is being used to boost private profit. Others may see this as the result of "state capture" by big business.

There are many reasons to question the decision of the government. The first is that its argument that the gas industry will be starved of investment if prices are not raised goes against the evidence, as senior and respected retired civil servant E.A.S. Sarma with much expertise in the area has argued. Second, the principles on the basis of which the new price has been arrived at by the Rangarajan Committee is open to question and not above suspicion of being part of a conspiracy to favour Reliance Industries Limited (RIL). Third, RIL has been charged with wilfully not meeting the production targets agreed to in its revenue sharing contract with the government, and the matter is now under investigation. Many believe that RIL is hoarding gas to reap higher profits once prices are raised. Giving it the benefit of a higher price when this issue is under investigation does seem unusual. Fourth, the government's claim that this will benefit the public sector oil companies as well does not sell, because other parts of the public sector, such as power producer NTPC, are expected to take a hit due to cost increases making the net impact on the public sector unclear. Finally, the UPA government's decision to announce the new price and implement it at the fag end of its tenure does suggest that it wants to be seen as having taken the decision to favour gas producers, including RIL. The allegation that there was a quid pro quo for individuals or organisations responsible for the decision is only a short step from there.

Even if all these strong reasons for concern over the government's decision were not there, suspicion of undue favour on the part of the government was more than likely. This is not just because of the controversies that have dogged Reliance's rise to dominance in Indian industry, many of which have to do with its ability to bend rules and swing government decisions in its favour. It is also because across a range of industries in all of which Reliance is not necessarily the dominant player, the state is seen as having shown undue favour to big business. Allocation of 2G spectrum and of coal blocs are just two other more visible examples of decisions that middle class India is convinced constitute evidence of an illegitimate or even illegal nexus between the state and big business in which the latter is the beneficiary and sections of the former on the take. All the more so since the evidence that the nexus between the state and private capital, to the "benefit" of both, has strengthened rather than eroded under India's neoliberal policy regime is too obvious to ignore.

This is not to say that state policy did not benefit Indian capital prior to liberalisation. Even during the Nehru era, now commonly dismissed as the heyday of the licence-permit raj, it was clear that policy implementation favoured big business which was able to garner a disproportionate share of licences, leading to increased industrial concentration and the strengthening of a few industrial houses that competed with each other, but kept out all new entrants. In fact it was only when the licensing regime was discredited and diluted that "new" entrants like the Ambanis could break into the charmed circle of Indian big business.

However, there are certain differences between what was observed at that time and what has been witnessed over the last three decades. First, most often the strength of the traditional business groups like the Tatas and Birlas did not come largely from a relationship with the state that involved a quid pro quo. Rather it came because of the ability of these groups to circumvent and/or subvert state policy and the failure of the state to discipline Indian capital, even in areas like tax evasion or avoidance. The dominant problem was "state failure" rather than "state capture". Business power in post-Independence India was not the result of cronyism but of the ability of the private sector to stand up to the state and the failure of the state to penalise errant business behaviour. A striking example of this was the ability of the leading groups to pre-empt a large share of the licences issued, even when they did not plan to implement them, and keep out new entrants. Second, while the traditional business groups were benefited by state policies such as protection, regulation of foreign investors (who would, otherwise, have swamped Indian business) and investment support from the development finance institutions, they did not get support in the form of state-provided access to near-free land, mineral and other resources and to large tax concessions, all of which became routine once economic reform began and it was declared that the role of the state was not to regulate private capital and build a strong public sector, but to facilitate and promote private investment.

One observed result of state capture is a sharp spike in profit margins and profit shares under liberalisation, not because of the operation of "market forces" but because of "state action". Thus, a feature of the neoliberal era in India, as elsewhere in the world, is the role played by the state in redistributing assets and incomes in favour of a small elite, including specially chosen business groups. There are many other ways in which this redistribution has been engineered. One obvious example is disinvestment. Not only has the government divested equity in some of its most profitable enterprises, but it has done so at prices that have been found (as in cases such as BALCO sold to Vedanta, IPCL sold to Reliance or Centaur Hotel, Mumbai sold to Batra Hospitality and then Sahara) to be way below the true value of the assets involved. Moreover, in many cases, under the policy of strategic disinvestment, business groups acquiring a minority stake of 26 per cent or more were handed over complete control of the company. In the case of VSNL, this allowed Tatas to access the large cash reserves that were available with the company to facilitate its own expansion. More recently, the public banking system has become a tool to ensure transfers to private capital. A study of the role of public banks in the case of Kingfisher Airlines is telling. Not only was the airline favoured with huge loans of around Rs.7500 crore, but when it became clear that its was not in a position to meets its debt service commitments, the debt was “restructured”, with lengthened maturity, better terms, additional financial support and the conversion of loans to equity. Despite efforts made after the company failed, little of this money has been recovered by disposing of its assets.

Fiscal policy and profits

The government has also favoured profit earners and contributed to the profit boom by providing them with a host of tax concessions. Revenues foregone through various concessions and tax preferences have become a significant part of fiscal policy. Although the Kelkar Committee Report on Direct Taxes (2003) had recommended reducing or eliminating such concessions while reducing tax rates, this has not happened. Indeed, while the tax rates have been reduced progressively since then, various concessions were also continued and then even expanded especially in the wake of the global crisis in Budget 2009-10. As a result, such concessions have grown significantly in value. For 2012-13, they have been estimated at a total of Rs 5,73,627 crore – as much as ten per cent higher than the total fiscal deficit of the central government.

These "tax preferences" include a range of measures - such as special tax rates, exemptions, rebates, deductions, deferrals and credits - that are provided in accordance with certain policy priorities of the government, and obviously affect both the level and distribution of tax revenues. As the Finance Ministry has noted, these tax preferences may be “viewed as an indirect subsidy to preferred taxpayers".

In the case of corporate taxes, all sizes of companies (by amount of profit) paid much less than the statutory taxes. However, the largest companies with annual profits of more than Rs 500 crore accounted for the bulk of the profits and the greater amount of the tax payable. Moreover, in 2011-12 for example, the effective burden of tax paid was among the lowest for them – only 21.67 per cent, substantially lower than the 26.26 per cent paid by smaller companies with less than Rs 1 crore of profits.

Arvind Kejriwal’s decision to target Reliance Industries is perhaps because its rise to dominance has been accompanied by much evidence of benefits derived from state support and favour. In that sense, the behaviour of the group epitomises the phenomenon of state influence and capture. But most of India’s leading business groups are part of this game. They have all benefited in more ways than one. The problem is not one bad egg, but a system that is rotten because of the regime of state intervention and regulation (or lack of regulation) that defines it. It is also rotten because associated with state capture are pay-offs to those in politics who facilitate and execute it.

Recognising this is important because the problem is not just of a corrupt Congress or UPA. The UPA government, especially in its second tenure, has earned the reputation of being one of the most corrupt in post-Independence history. Not surprising, since the Congress is the one that launched liberalisation in India and pressed ahead with it. But, the NDA too swears by neoliberal ideology (ostensibly combined with a religious “nationalism”, as if that were possible). Not only does its leading element, the BJP, have an openly pro-business tilt in terms of its origins, but whenever and wherever it ruled it too has unduly and often illegitimately favoured big business. One needs only mention disinvestment under the NDA and everything economic under Modi in Gujarat to illustrate this. If there is any reason why the BJP and the NDA can claim to be less of a participant in the process of state capture by big business it is only because it has been far less responsible for state policy than the Congress because of its briefer stint in power. Yet it is not clear whether the pay-offs it earns is any less.

The tragedy for these political parties and formations is, of course, that in the game of state capture, with or without a quid pro quo, the rules that apply to those in politics and those in business differ. For the politicians, playing the game requires getting all big business groups to see them as the best bet in the neoliberal game. In the case of business, however, you need to be with whoever is likely to sway India’s electorate and return to power, switching sides as the political mood changes. The ease with which big business has swung in favour of Modi and the BJP in recent times, given the expectation that the latter have a much better chance of forming the post-election government than the Congress, is evidence of this. Perhaps for the Congress the only cause for comfort is that this betrayal in itself may not determine the actual election result.

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