

Bowing to necessity

The government's bank recapitalisation scheme may have some technical merits. The previous government, with an unconscionable combination of cronyism and inability to assess risk, had left the banking system in a deep mess. So drastic corrective measures were needed to solve the twin balance sheet problem. Whether the bank recapitalisation achieves that is still an open question. Much will depend on the details of the scheme. Does it tackle the magnitude of the problem? What will the actual costs be? Will the institutional reforms government has promised be realised? It should worry us that there is so much spin and euphoria even before the details are made available. But more than the technical issues, this episode is an interesting window onto the relationship between state and capital in India. And alas here, the more things change the more they remain the same.

What does the politics of recapitalisation signify? One way into this question is to ask the following: If bank recapitalisation is as painless and a relatively costless accounting exercise as it is being presented, why was it not done earlier? After all, there is a precedent for this scheme. Rather than being radical, it is the classic "defer all the hard decisions, put band-aid" playbook of the Indian state. One answer is of course demonetisation: The banks are now flush with cash. But the other, more sobering answer is that the Indian state is unwilling or unable to bring big Indian capital to heel, and is now giving up. From a point of view of preventing moral hazard, sound politics, and principles of justice, it would have been a lot more credible to first decisively move on the NPA problem.

This has two aspects. First, the government has to demonstrate the capacity to discipline big capital; it has to demonstrate the capacity to penalise at least some big companies for their brazenness or their incompetence. Instead of a moralised, all pervasive, fear-producing crusade in the name of black money that was carried out on the backs of ordinary Indians in the name of demonetisation, the ability to smartly go after defaulters would have been far more reassuring for the future of state-capital relations.

Second, in many cases renegotiation of the projects is required. There is a myth being peddled that renegotiations are difficult because no banker or government official will sign off on a haircut they will inevitably have to take. They will be subject to scrutiny, and such deals may not pass democratic muster. But this is, at best, a half-truth and at worst, an ideological mystification that is letting big capital go scot-free. For the truth of the matter is India big capital is still holding out for unrealistic returns, and wants to shift the burden of haircuts on the government or the consumer.

The most egregious example of this is the real estate sector (closely related to infra), where tens of thousands of consumers with their life savings have been left stranded by the government because it has not been able to get real estate companies to restructure their assets or protect ordinary consumers. The courts have now begun to intervene.

The government has, to be fair, initiated steps both on disciplining-the-companies front and on renegotiation. But there is still a big question mark on the credibility and effectiveness of these processes. The government will still be left with what we might call the twin legitimacy problem. If it goes after big capital rigorously, it risks derailing growth; if it does not, it will lend credence to the perception that the big sound and light show over black money was essentially to take from the poor to protect the rich. And the sequencing of measures sure makes it look that way. Recapitalisation may be necessary. But the fact that recapitalisation has happened before real NPA reform and disciplining of errant companies will give credence to the impression that ordinary Indians are being imposed upon, while big capital is still protected.

Whether this recapitalisation will lead to growth and when is an open question. More than the alleged credit slow down, tax uncertainties, supply-side shocks, the fact that savings of middle-class Indians are stranded in non-delivered investments like housing, and the uncertain costs of formalisation are probably bigger factors. So the jury is out on the growth gambit. That the government bets on another old play, increase investment in roads, suggests it has also run out of diagnosis about why private investment is not picking up.

But still, the recapitalisation should leave us uneasy about how much the balance of power in Indian society is still skewed in favour of big capital, not the small entrepreneur or ordinary investor. This is underscored in two symbolic dimensions of the measures announced. When banks and big capital mis-price risk or engage in cronyism, the problem can be fixed by "accounting" tricks. But when it comes to protecting ordinary people, especially farmers, from risk or investing in health and education, it leads to worries about fiscal deficit and sovereign downgrading. The resentment this contradiction generates will be sharpened. The only consolation for the government is that the Congress cannot make political hay of this recapitalisation, since it created the mess in the first place.

The second symbolic dimension is this. The government has announced steps to ensure that MSMEs do not face working capital shortage because of delayed payments by allowing trade in receivables. This may ease the problem. But it symbolically underscores what is wrong with state-capital relations in India. If a small business is owed a legitimate payment for services rendered of say, rupees hundred, their only option may be to sell the due recoverable at a discount.

In short, they have to pay a persistent haircut to big capital, because they cannot have payments enforced. On the other hand, big capital can default and still hold out for a good deal. The government may have saved the banks, but whether it can structurally transform the nature of Indian capital or the state is not entirely clear. The government has bowed to necessity; whether it will lead to credibility or justice is an open question.

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