

Operations of the Market and the State in India: Limitations and Failures

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Indian economy has been growing in the recent years at growth rates oscillating widely, as revealed by the Official estimates published periodically. The differences are varying cyclically, based on many factors on which State has very little control. Inflation has been throttling the lower strata of the Society mercilessly, compared to those of the higher income groups, who patronise the five-star culture. The Market, with all its imperfections resulting from regulation, de-regulation and partial regulations, has been behaving strangely. Poverty estimates also make different numbers of people moving below or going above the ubiquitous poverty line, temporarily or otherwise. It is simple for those, who estimate, but pathetic for those face it.

Emerging India is a bundle of contradictions. According to the recent World Bank study, *The State of the Poor: Where are the Poor and Where are the Poorest?*, the number of extremely poor people had declined from half the world's population in 1981 to one fifth in 2010. But one-third of the world's poor live in India. Malnutrition and starvation continue to pester the poorest of poor in many parts of the country. With a marginal increase rural incomes, when the poor started eating a little more food articles than what they could afford to purchase earlier, food prices shot up. Where the marginal propensity to consume is high, it is but natural that a little more money would be spent on food articles. The over-fed economists abroad blamed the poor Indians for tilting the demand curve of food articles causing thereby global inflation. At the same time, India leads the world in total rum consumption. It is estimated that more than 20 percent of the alcohol manufactured in the world is consumed in India annually.

The latest World Bank Report *A Comprehensive Analysis of Poverty in India* by Arvind Panagariya and Megha Mukim (2013), after analysing the recent controversies in India regarding the choice of poverty lines, presents a positive picture of reduction in poverty ratio. Inter-

state differentials in the decline in poverty ratios, as well as the differences among religious groups and social groups also are estimated in detail. Kerala is one of the states, where both the rural and urban poverty ratios are the lowest.

Kerala, God's own country, has many other interesting features. Copious remittances from the Gulf contribute largely to the better living conditions in the state. Literacy ratio is one of the highest in Kerala state, where banks also claim to have made visible achievement in financial inclusion.

This state's share in the sale of alcohol is 16 percent, largest proportion among all the states in India. "The state also has the highest wages in India for many manual jobs. Even a [builder] is getting paid a lot...if they get 500 rupees a day, they can spend 200-300 rupees drinking, the bar owner in Thrissur, says of his customers" observed *The Economist* in an article: *Drinking in Kerala- Rum, Rum Everywhere* (*The Economist*, 2013).

The pattern of household expenditure is changing very fast across all income groups, adding to the bundle of contradictions the emerging Indian economy exhibits. TVs and mobiles could be seen in good numbers in jodpries surrounded by garbage dumps and open drains. Elegantly illuminated show rooms of foreign cars and scooters of wide price ranges are coming up in even tier-two cities.

India produces one of the largest numbers of films annually, competing with Hollywood, both quantitatively and qualitatively. First day releases of high-budget pictures are becoming widely publicized events, collecting over Rs.100 crore on the opening day. Though the multiplexes coming up with multiple screens in big cities, keep the earlier front-bench patrons away, young ITians, who have flexible office timings have become the new patrons. Old cinema theatres have yielded place to high rise buildings and shopping malls.

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India no more lives ONLY in villages. Out-migration of unskilled farm labourers, spreading into far corners of the country has become a reality. Language is no more a barrier and distances do not matter. Boys from Manipur could be seen working in almost all Udupi hotels in many cities in Maharashtra and Karnataka. Improvement in literacy levels has resulted in the youngsters shunning to pursue their hereditary occupations like carpenters, barbers and washer men. Migrants from Bihar, Uttar Pradesh and Rajasthan quietly fill up these vacancies in other states. It is the market force which provides the scope for such changes. This process is not initiated or supported by any official or institutional agencies. The changing conditions in the labour market in different parts of the country have induced and supported this process. The composition of the society slowly changes, acquiring cosmopolitan stature. The State remains a mute witness to this gradual process of socio-economic change.

Without going deeper into an analysis of this changing process, it is proposed to take up only three issues, where the State's interventions or lack of it, in Marketing have direct impact on the well-being of the Society.

- 1. State Monopoly in Marketing Alcohol: Intoxicating.**
- 2. State's Lethargy and Price Rise: Not Convincing**
- 3. Market Theology and Micro Finance: Incongruous.**

The implications of State monopoly in marketing a product like alcohol, on the welfare of the Society are examined first. The hardships caused to the Society due the State's lethargy in regulating onion prices are explained then. Thirdly, the exploitation of the poor borrowers by micro-finance institutions, when the State takes shelter under its allegiance to market theology, is analysed. These three issues are briefly explained, without marshalling an array of data to substantiate.

State Monopoly in Marketing Alcohol: Intoxicating

Some of the state governments in India, which are unable to curtail abnormal increase in their unplanned

expenditure, turn to sell liquor, among others, to raise revenue. The civil Society approves this silently. Those in power, irrespective of party affiliations, do not oppose this; the State has, after all, to find enough funds to finance also the foreign jaunts of the elected representatives. Selling a harmful commodity like alcohol to reduce budgetary deficit is certainly not desirable means of financing the other developmental programmes. Ends cannot always justify the means adopted. Growing dependence on alcohol revenue is an unfortunate development in our fiscal management.

"The Kerala State Beverages Corporation, a state-owned monopoly that controls all liquor shops and wholesale booze sales to bars, is booming. KSBC's taxes contributed over \$1.2bn to Kerala's coffers in 2011-12, accounting for a fifth of the state's overall revenues" revealed an interesting article in India File in BusinessLine recently. (Basheer K P M 2013). Nearly 22 percent of the state revenue comes from the bottle.

Kerala's three neighbouring states-Tamil Nadu, Karnataka and Andhra Pradesh- also have similar monopolies. In Tamil Nadu, the Government-owned Tamil Nadu State Marketing Corporation, which has the monopoly of selling Indian Manufactured Foreign Liquor in the state, has paid to the Government, Rs.21,800 crore.

Karnataka does not lag behind in filling up generously its exchequer with the money collected from wholesale trading of liquor. The excise revenue is not less than 20 percent of its total revenue. Some other states handle only wholesale trade in alcohol leaving the retail trade to the private traders, making them partners in increasing the number of outlets for selling alcohol. Bars are allowed to remain open for 11 hours a day and seven days a week.

As if to add insult to injury, our Exim Policy allows hotels to use five per cent of their Forex revenue to import alcoholic drinks without duties. While the country continues to have adverse balance in international trade, we continue to import non-essential commodities like alcohol and gold. India has trade deficit with as many as 81 countries in the world. And the trade deficit is \$191.3 billion in 2012-13.

The State exercises its authority to have the monopoly of alcohol trade, regulating the Market as a result. The growing revenue from sale of alcohol is intoxicating the State to raise more revenue inducing indirectly higher consumption. The Society is made to pay a price: spreading ill-health, breaking family life and increasing violence. Sale of alcohol increases annually at a rate of 8 percent, much higher than the rate of growth of the country's GDP. The State is hard-pressed to find enough resources to provide basic health facilities. National Drug Dependence Treatment Centre at All India Institute of Medical Sciences.(AIIMS), cannot train enough doctors throughout the country to treat the growing number of people affected by alcohol abuse.

Among its Directive Principles, the Indian Constitution does include the prohibition of alcohol. But alcohol policy is devolved to individual states and states consider alcohol business as Kaamadhenu in their search for raising revenues. In addition to this, there exists a powerful alcohol lobby, which is strong enough to influence the political process. It is not a secret that in the periodical battles for ballots, bottles also have a role to play some extent.

There is a Gujarati saying epitomizing the dangers of the State-Market nexus. It says:

Raja bane bepari, Praja bane bikhari.

Its free translation would be as follows:

When the King becomes trader,

Subjects (people) become beggars

Alcohol abuses manifest in the growing number of separations and divorces in families, poor and rich. They cause emotional hardships and trauma, which cannot be measured in terms of money. The money raised by the State through sale of alcohol cannot compensate the sufferings of families in distress.

State monopoly in marketing need not be universally an undesirable feature. But the state has many other important functions to attend to. Managing public health effectively ought to be its top priority than raising revenue by selling a product, which is injurious to health. It is more than a mockery that the State directs all TV channels and film producers to insert a jargon Consuming Alcohol is Injurious to Health, whenever a scene of people drinking, is shown on the screen.

State's Lethargy and Price Rise: Not Convincing

In recent years, an obscure farm product like onion has been causing concerns to the State and housewives repeatedly. This tear-jerking product was also responsible for bringing down an elected government earlier. Incidentally, India is the second largest producer of onion and accounts for a 19 percent share of the global onion production. Maharashtra and Karnataka are the major onion producing states in India and contribute nearly 45 percent of the total output of onion in India.

While nature determines the size of onion output annually, market manipulates the quantity available to the consumers. The primary producers are normally hit by the glut in the market, whenever there is a bumper crop. They are also the losers, when there is a crop failure. It is the traders- the hoarders specially - who make money, when the State remains indifferent. When forced to act, half-hearted steps are announced by the State either to curtail export of onions or to liberalise its imports, as short-term measures.

Hoarding by traders having strong political connections is the root cause of this feature of abnormal increase in onion prices. Their political clout is so strong that the State does not take drastic actions to curb this tendency. Hoarding of onion continues in the major onion markets by traders, who have political support. The State-supported marketing agencies like NAFED (National Agricultural Cooperative Marketing Federation of India) are ineffective as strategic market players. This marketing agency, however, is not associated with onion trade. It is reported that the loans given to it a few public sector banks have turned to be NPAs. (Business Standard, 2013)

Chanakya's frown on hoarding is explicitly incorporated in his Arthashastra. In the 4th part of his magnum opus, strangely titled as "Suppression of Criminals", the second chapter is on "Keeping a Watch over Traders". He has stipulated that, "For traders, who by conspiring together, hold back wares or sell them at a high price, the fine is one thousand panas". When compared with the range of fines stipulated for many other offences, this amount is quite high.

When India emerged as an Independent nation, food shortages and black-marketing were among the various problems faced. Pandit Nehru in righteous indignation against these irritants, reported to have made an outburst; Hang the black-marketers at the nearest lamp post. However, no record is available about the executions made on this count. Perhaps, the lamp posts were saved from facing the ignominy of illuminating the dead bodies of those, punished for their black deeds.

In a recent study of the gyrations in onion prices, Competitive Assessment of Onion Markets in India, undertaken by the Institute of Social and Economic Change, Bangalore, it was recommended that, " In view of the inefficiency in the supply chain in Maharashtra and Karnataka, the Government and the Competition Commission of India should take steps that would lead to a healthy competition, which has the ability to reduce market imperfections as well as improve the welfare of all the actors involved in the market channel (producer to consumer). To fulfill this, it is recommended that necessary changes should be made in the APMC Act in line with the Competition Act of 2002"

Ambivalent policy of the State is responsible for the uncontrolled rise in onion prices. During the current year, for example, when the total onion output was lower by 4.89 per cent and exports were higher by 17.39 per cent over the previous year. Though onion prices have been rising swiftly, 7 lakh tonnes of onions were exported between April and August this year. Traders' lobby is certainly stronger than the poor housewives' grumblings.

Onion does not come under the Essential Commodities Act of 1955. Hoarders cannot be controlled in the absence of such powers vested with the state machinery. The hoarder-politician nexus is very strong. The State, however, cannot remain content with adopting fire-fighting methods only when prices of onion or other food articles rise sky-high. It has to put in place a mechanism to curtail price rises by facilitating the development of transparent marketing policy supported by better storage facilities.

Market Theology and Micro finance: Incongruous

In classic Indian literature in any language, the village moneylender was caricatured as a rapacious exploiter. His ruthless operations have lent credence to this belief. He was charging exorbitant interest rates in addition to the more than adequate collateral security demanded. Inevitably therefore he is being replaced by institutional lenders - banks and cooperatives-mandated to lend at rates, sometimes lower than their cost of funds.

Moneylender was totally denounced for the high rate of interest charged by him and the strong arm tactics adopted by him in recovering his dues. To replace him, by institutional credit agencies, new purveyors of rural credit have been introduced and supported by the State almost for a century now. The cooperative credit societies were the first agency to be created for this purpose. Rural branches of public sector banks and the gramin banks were directed to offer credit at much lower rates charged by money lenders. NABARD recently came out with a scheme to encourage the gramin banks to replace the money lenders' credit by swapping it to have money lender free villages. It is an arduous task, as money lenders have deep roots in rural societies, having been operating for centuries. The pauperization of India peasantry is an historical legacy from the alien rule. (Thingalaya 2013.a). State operating through the Regulator has largely regulated the interest rate structure of banks.

Differential interest rates are fixed for the small borrowers classified under the priority sectors. In 1972 a specific credit scheme called Differential Interest Rate (DIR) scheme was introduced to lend credit to the low income groups at a concessional rate of interest of 4 percent, when the Bank Rate was 8 percent, Public sector banks were directed to lend one percent of their total credit under this scheme. Banks could not achieve the target, though the scheme continues to be in operation.

The new entrant to the field of small credit in the recent years in the micro-finance institution (mFI). It has angel investors and the tacit approval of the State. Imitating money lender, mFIs charge the highest rate of interest with impunity. They take shelter under the canons of

market theology, pinning their faith in the invisible hand of market force, which is believed to be deciding the interest rate. Monetary pundits, who were pleading earlier for reduced rate of interest, are now supporting the market theology; interest rates are determined by the market forces. The argument that interest rate charged by mFI is lower than that charged by moneylender is not a sufficient justification for charging rates much higher than that charged by banks (Thingalaya, 2006). The crude manner in which some of them have stepped up their recovery rate has created undue hardships to the debt-ridden poor farmers, resulting in the increase in suicides.

The financial market in India is not free from regulations, partial and total in specific cases. Export credit is lent by banks at rates much lower than that charged to the farmers.

The MFIs, however, do not come fully under the purview of the Regulator at present. Though the Government of India is planning to bring out an act to regulate the functioning of MFIs, there appears to be strong reluctance on the part of the authors of the proposed act to prescribe a cap on interest rates. While the moneylender, crude in his dealings, was despised and disliked universally, the sophisticated MFIs are treated as the saviors of the poor. Does it matter, if the poor are required to pay more for the services rendered?.. the argument goes.

The interest rates charged by the MFIs are competing with those of the moneylenders', on the higher side. They are charging anywhere between 24 to 36 percent per annum, with very few exceptions. And they have no hesitation in declaring that they are delivering this high cost credit at the door-steps of the poor borrowers. If the SHG member has to borrow at this higher rate, can she ever succeed in clearing her old debts?

The rural borrower is no more interest-insensitive; he is aware of the interest rates charged by various credit agencies. He tries to swap his high interest bearing loans by borrowing from SHG. If SHGs have to borrow from MFIs at higher rates, they cannot lend to their

members at lower rates. Then the members cannot liquidate their existing borrowings from money lenders bearing higher interest rates. Their indebtedness is likely to be perpetuated under these circumstances.

The Reserve Bank, which was regulating the interest rates of bank advances very meticulously with a wide range of rates, cannot afford to be a silent spectator, when the poor borrowers are exploited openly. Secondly, the MFIs should voluntarily adopt a social audit to assess whether the interest rates charged by them are justified. While viability and reasonable margin of profit are fundamental prerequisites for financial institutions, encashing on the misery of helpless borrowers has to be avoided. It may be noted that there are also some MFIs, whose interest rates are not higher than 12 percent. And they are viable and have strong bottom lines. The secret of their success is a very lean administrative set up, where the executive remuneration is not luxurious.

The track record of some MFIs of Andhra Pradesh in forcefully recovering their loans from the poor defaulters is replete with scores of suicides committed by helpless borrowers. Perhaps these MFIs would have taken a clue from one of last uncivilized means suggested in Manu's mandate for recovery. (Thingalaya, 1999). A recent development in this sphere appears to be very positive, if it really becomes effective. It reported that "five MFIs have received certification for client protection from Smart Campaign, a global initiative to incorporate strong client-protection practices into the microfinance industry. The certificate is given on the basis of principles like pricing, transparency, fair and respectful treatment and prevention of over-indebtedness." (Business Standard 2013). There are many other MFIs, which are yet to get such certificates. Also it is not known, whether the certificate ensures that the exorbitant interest rates are controlled or substituted by other charges levied by them.

It is necessary to examine as to whether micro-credit could be a permanent cure for eliminating the economic hardships suffered by the poor or it could be only a

pain-killer. MFIs tend to propagate a view that they are eradicating poverty through micro-credit that they lend. (Sambamurthy 2011). Sustainable development in the income generating activities is very difficult to achieve in a short span of time. And certainly credit alone is not the engine to facilitate this process. There are reasons to believe that the Bangladesh experiment of gamin bank is not a great success in lifting all the borrowers above the poverty line permanently.

Gramin banks have proved to be more suitable micro credit operators in the rural sector than the high profile mFIs. Karnataka Vikas Grameena Bank, for example, has emerged as the highly successful rural credit agency, lending to large number of small borrowers at reasonably lower rates of interest and still making good profit. Covering 2310 villages through 524 branches and handling a total business of Rs.13,015 crore, it has made a net profit of Rs.194 crore in FY2013, the highest among the gramin banks in India. On the top of it, its net NPA ratio is zero (Thingalaya 2013).

Gramin banks are in the public sector, except for one bank out of 57. Their operations are regulated and supervised by two regulators- Reserve Bank of India and NABARD. Serving the rural society being their avowed objective and the very basis of their formation, they are extending credit facilities at reasonable rates. The MFIs on the other hand, being promoted by the private sector, maximisation of profits is their objective obviously. As their cost of operations is very high, they cannot but charge higher interest rates. However, since there is a cheaper credit agency - gramin bank - having proven track record, should the State permit the mFIs to exploit the poor?. No doubt, mFIs have a role to play in a credit-starved Society like ours, but not at gun point.

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