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MNC entry is a Trojan horse for Indian industry

The perception that the MNCs would bring more capital and technology to facilitate the growth of Indian affiliates is erroneous. An MNC which does not pay a reasonable price for buying shares in the first instance can scarcely be expected to bring funds in, says Uttam Gupta.

GLOBALISATION is proving detrimental to Indian industries and the national economy. Although, even prior to 1991, MNCs were having their presence in India through their Indian affiliates, they were, however, minority partners with equity holding below 50 per cent. Since 1991, however, they have been allowed to raise their holdings up to 51 per cent and beyond.

The MNCs have responded enthusiastically, with a majority raising their stake by buying heavily discounted shares through the preferential allotment route. Needless to mention, the government stands a mute spectator. It came out with the necessary directives only after the virtually free takeover operations were successfully completed.

In the process, the affiliates were even denied much-needed funds for expansion and diversification; funds that were legitimately due to them purely on the strength of their fundamentals. Besides, it was a clear loss to Indian shareholders by way of losing control over management apart from a reduced share in the overall profits of the affiliate.

Why did the government permit a majority stake to the MNCs? The perception was that the latter would bring more capital and technology to facilitate the growth of Indian affiliates and, thus, improve their cost competitiveness. This is erroneous. An MNC which does not pay a reasonable price for buying shares in the first instance can scarcely be expected to bring funds in.

The actions of the parent company do not inspire confidence. As regards technology transfer, a majority of the Indian companies, including MNC affiliates, have only met with disappointment so far. And, this is more so in areas like drugs and pharmaceuticals where latest technology is needed the most.

As if that was not enough, the government also permitted MNCs to enter directly by setting up 100 per cent subsidiaries. Full ownership of a company is far better than investment in an affiliate in which Indian shareholders are also partners. This is all the more so when the sphere of operation is predominantly the consumer goods sector.

It offers the possibility of most lucrative business in India. With less investment, profit margins are unprecedented, thanks to buoyant demand from the huge middle class, many of them having a lot of surplus money (included unaccounted) and who are even willing to pay any price for a good brand.

The removal of restrictions on repatriation and consequential assurance of profits/dividends in foreign exchange, has further added to the charm of setting up 100 per cent subsidiaries. With free repatriability, why would the MNCs have interest in an affiliate where the profits have to be shared with Indian shareholders?

Presented with a honeymoon, the MNCs have virtually flooded the Indian territory by setting up fully foreign owned companies. In many cases, these have even been funded by riding rough shod over their Indian affiliates (funds raised by selling their holding in a booming market at high prices). Having done so, they have launched a neatly orchestrated gameplan to withdraw the support base of Indian affiliates with the ultimate objective of unseating them.

Most profitable businesses have been transferred to 100 per cent subsidiaries; so much so, even infrastructure, dealership network, brand image etc — developed at a heavy cost to the Indian affiliate — is being used to subserve the cause of the 100 per cent foreign. Indian shareholders in the affiliates cannot say 'no' to all his because they are now in minority.

Is this the kind of scenario that we anticipated when India decided to go global? Any policy change has to address a basic question as to whether it will benefit the national economy. The test is in relation to the implications by way of foreign exchange earnings, contribution to the overall rate of industrial growth, the addition to income and employment and improvement in the living standard of people and quality of life.

On the foreign exchange front, one need not do a detailed profile of the operations to conclude that, on a net basis, the foreign exchange balance-sheet of the 100 per cent subsidiaries will be substantially negative. This is because initial investment is less, profit margins are hefty and export commitments small or even negligible.

True, such has been the story of the Indian affiliates even as the underlying fundamentals governing their entry in the first instance, and operations thereafter, have been broadly similar. The entry of 100 per cent subsidiaries will further aggravate the trend.

On income and employment, already, the situation has worsened in the Indian affiliates with majority control passing to the MNCs. It will become serious consequent to virtual annihilation/elimination of the former at the hands of the latter in its original incarnation.

The indirect effect too, cannot be wished away as in terms of sourcing raw materials, components, spare parts and related pricing and procurement policies, the attitude of the 100 per cent foreign subsidiaries is bound to be detrimental to the Indian industries in the small scale sector.

Encroachment into areas exclusively reserved for the SSI and resultant adverse repercussion on employment is also not ruled out.

As regards industrialisation, it cannot be anybody's case that 100 per cent foreign subsidiaries will contribute more than their Indian affiliate or a 100 per cent Indian company. As a nation with self-pride, we would prefer to have growth through the last category and if necessary, through the second preferably with minority equity holding by MNCs. This is not just dogma but a practical economic necessity.

The critical question is whether MNCs are committed to continued rapid industrial growth in India? The answer is a categorical 'no'. Their commitment is to profits. So long as they can maintain good profits and are able to repatriate, they will stay. The industrial development that follows, will only be incidental.

In a nutshell thus, a highly inequitable and discriminatory situation has developed in which the Indian industries as well as the overall economy are subject to exploitation by the MNCs. There is an urgent need for a relook a the policy in regard to the 100 per cent foreign subsidiaries.