The Observer of Business and Politics May 31, 1996

Need for selectivity in MNCs' entry

The new government should focus on laying down priorities for foreign investment keeping in mind the overall objectives of economic policy and sectoral needs, says Uttam Gupta.

CONSEQUENT to opening of the Indian economy to foreign investment, MNCs have entered in a big way. In view of the potential to make good profits, the consumer goods sector has attracted them the most. Initially, they came riding on the joint venture partners. Now, following permission to set up 100 per cent subsidiaries, the MNCs have preferred this route for investment.

The attraction of the small scale sector is greater in view of the much lower investment requirements. Although, because of the policy of reservation, direct entry is not possible, some of MNCs have managed to come, taking advantage of the enabling provision, e g 75 per cent export obligation or existing loopholes in the definition of items reserved for the SSIs.

Investment in the infrastructure is, however, not so attractive. This is because the investment requirements are huge, time for completing the project is long and the MNCs have to wait even longer before the project starts yielding return. Added to this, is the problem of timely and full payment. This is especially true of investment in the power sector wherein electricity has to be sold to the SEBs whose payment record is not credible.

Lack of clear-cut and transparent policy and the requirement of numerous clearances make the MNCs wary of investing in infrastructure. This is despite the government allowing them to invest on 100 per cent ownership basis. Ever since the power sector was thrown open, not even a single power plant has come up in the private sector. Progress in basic telecom is extremely slow.

On the basis that we are short of capital, the outgoing government wanted foreign investment to fill the gap. But, this was not backed by a clear-cut and coordinated policy. Even the priorities were not laid down. Where do we need the MNCs and where do we not need them? And, within each area, to what extent, should they be permitted to invest? These vital questions have not been addressed.

All that was put in place to guide flow of foreign investment is the Foreign Investment Promotion Board (FIPB). In the absence of a clear cut policy, its functioning is discretionary and lacks transparency.

The new government should focus attention on laying down priorities for foreign investment, keeping in mind the overall objectives of economic policy and sectoral needs. Our aim at a rapid growth of the GDP should lead to increasing employment and reduction of poverty. This is necessary to maintain social harmony.

In the SSI sector, the objective is to achieve growth by setting up a large number of industries on small scale, employing labour-intensive technologies and a better distribution of income. Considering the risk inherent in import dependence, the emphasis has to be on indigenously developed technology to ensure

sustained growth. Technology support from the MNCs is neither desirable nor sustainable.

From investment angle also, the involvement of MNCs is totally unnecessary and unwarranted. The existing ceiling for the SSI sector was Rs 60 lakh and even after the revision, this stands at Rs 2 crore. It cannot be our case that the SSI manufacturers cannot undertake this investment. Wherever they need support, funds should be made available by financial institutions and banks.

On the export front, the SSI sector is already earning the maximum amount of foreign exchange for the country. It can do even better if only the government provides the much needed support through improvement in infrastructure, increase in availability of credit and simplifying various rules and procedures especially at the ports for speedy handling of the cargoes. Additionally, information on potential markets abroad, consumer preferences and product standards insisted upon by regulatory bodies will also be helpful.

Even as the MNCs have nothing more to give in addition to what we have and what we are capable of doing on our own, their entry in the manufacturing of items reserved for the SSI units will seriously undermine the viability of the existing units and thwart the chances of more such units being set up. This will throw workers out of jobs, not to talk of no increase in employment.

In the consumer goods sector, we may need the support of the MNCs especially in view of substantial investment requirements and the intensity of the technological input. However, without the lure of significant equity holding, it may not be possible to attract them. But, if you go too far, i e majority holding or even permitting 100 per cent equity to MNCs, there is a danger of our own industries getting affected. Besides, this may have serious adverse effect on employment, foreign exchange outgo and social order.

For any given level of growth, apart from the capital-labour intensity of the manufacturing process, employment depends on who the manager is. The MNCs philosophy is to have a trim labour force. They are also actively involved in mergers and amalgamation which lead to loss of jobs. Clearly, permitting majority holding to MNCs is not conducive to growing employment opportunities.

The impact on the foreign exchange due to their operation here will be substantially negative as the outgo by way of repatriation of profits and on import of items of machinery and spare parts, far outweighs inflow through exports as the MNCs sell mainly in the Indian market. This may even affect essential imports, e g crude oil, POL, fertilisers etc, and, in turn, the overall development.

We also need to consider the impact on the social fabric. The salaries in the MNCs for equivalent levels are several times more than in Indian companies. These income disparities may give rise to class conflicts, spread of consumerism and blatant display of extravaganza.

In infrastructure, considering its inadequacy, massive requirements of funds for its development to support industrial growth and the need for advanced technology, there is a strong case for seeking large scale investment by the MNCs.

There is an urgent need to formulate a clear-cut and transparent foreign investment policy supported by comprehensive guidelines. So long as the foreign companies are conforming to these guidelines and overall intent of the policy, their entry should be automatic. In line with the policy of reservation for the SSI, the MNCs should be completely debarred from entering this sector.

In the consumer goods sector the MNCs may be allowed only through the JV with Indian companies preferably on 50:50 basis. While giving adequate inducement to the former, this would also safeguard the interest of the latter, besides reducing the risk of unemployment and heavy foreign exchange outgo.

In infrastructure, the policy may allow investment by MNCs even up to 100 per cent. However, to facilitate their entry, the government should amend antiquated laws, reduce the number of approvals required, set time limits for giving approvals and bring transparency in the policy and administrative guidelines.