PRAGMATIC OPTIONS

Of Meltdown and Opportunity

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The global meltdown is spreading as expected. Prices of agricultural commodities are already heading south. Wheat futures for December delivery are down 60 percent from last year. Prices of corn and soya bean are also declining. The main reason for this is less biofuel production. High price of oil had encouraged the use of corn and sugar for production of fuels in a big way. This had led to diversion of land for these crops and reduced production of wheat and other food crops. The recent decline in price of oil has reversed this trend. Farmers are coming back to food crops leading to increased supply and lower prices. This decline in price is likely to persist for some time because the meltdown is likely to be a long affair. The price of oil had peaked because of combined demand of developed and developing countries. The developed countries are unlikely to regain their purchasing power anytime soon because they will continue to face tough competition from India and China. In the result, the price of oil is not likely to hit the roof and, accordingly, the price of food is likely to remain low.

This low price of agricultural commodities is a global phenomenon and will encourage imports into India. The Government must provide protection to domestic farmers from these cheap imports. The Government had removed import duties from palm oil to rein the prices. These import duties should be re-imposed immediately to protect domestic oil seed producers from cheap imports. On their part, Indian farmers should try to penetrate global markets that were being catered by the developed countries till recently. For example, Holland is presently supplying flowers and Australia is supplying cheese. Purchasers of these commodities in America, Africa and Asia will look for cheaper substitutes as their purchasing power shrinks. India must provide a low-cost alternative to these products.

The impact on India's manufacturing exports will certainly be negative. Presently India is exporting garments, steel and minerals in large quantities to the developed countries. These exports will come under pressure as the purchasing capacity of the developed countries shrinks. But the goods purchased by the richer people such as jewelry and embroidered gowns will be less affected. A fashion expert from Mumbai says the fashion sector has not been affected at all by the meltdown-at least as yet. In fact, suppliers have added customers. Reason is that a meltdown hits the common man hard while the rich are hit only softly, if at all. The worker loses his job and has no money to buy new garments. But the personal expenditures of the businessman constitute a fraction of his total revenue, hence they are less affected. One does not hear of a businessman traveling in bus instead of private car due to the recession. This means that the market for luxury goods will be less impacted. In fact, this may open a window of opportunity. The rich will try to maintain their present standard of living and look for cheaper substitutes of their high-end purchases. For example, Sheikhs from Kuwait go shopping to Harrods in London. They will look for cheaper substitutes if the quality and appearance is guaranteed. Therefore, Indian businessmen should try to export low-price substitutes of high-end products like Bose speakers, Nokia handsets and Jaguar cars. India should try to establish an international chain of luxury stores like Harrods in oil-exporting countries, in particular.

Simultaneously, Government of India should move to protect domestic markets from cheaper imports. Other developing countries will be forced to reduce the prices of their exports of garments and other commodities as the markets in the developed countries shrink. They will try to export to India. On this issue, the Government will have to choose between two opposite considerations. On the one hand, domestic consumers stand to gain by access to cheaper imports. On the other hand, Indian producers will go out of business if cheap imports are allowed. The Government must protect the Indian producer first and consumer later. What is the use of a cheap frock displayed in the shop window if one does not have the money to buy it? This is not the time to hold on to free global trade. A crisis situation requires a response that is out of the normal just as the patient is given oxygen. Instead of trying to provide cheap Ganesh-Lakshmi made from plastic in China to the Indian consumer, the Government must move to protect the livelihood of the Indian potter who makes more the expensive Ganesh-Lakshmi.

The infrastructure sector will come under increasing pressure. Less foreign investment will be forthcoming here. The reduction in domestic growth rate will also lead to reduced demand for highways, airports and electricity. Therefore, instead of blindly continuing to add to capacity of these facilities, effort, must be made to improve the quality of existing infrastructure with lesser investment. The businessman does not establish new factories during recession. The same applies to infrastructure. The ultimate trick lies in matching supply and demand. Increasing supply of infrastructure is not very helpful when demand is less. It does not help to reduce the toll rate on the highway when people have no money to buy petrol for their cars. Effort must be made first to increase demand by putting more purchasing power in the hands of domestic consumers. Large infrastructure projects must be put on temporary hold till demand revives. The money earmarked by the Government for investment in infrastructure should be diverted to giving tax breaks to individuals or reducing excise duties on goods consumed by the common man such as rubber slippers and note books. This will revive demand and in the next cycle the country can continue building the infrastructure.

The impact on services sector will be less adverse than on agriculture and manufacturing sectors. India's service exports are geared to supporting production in the developed countries. The medical transcription services provided by Indian BPO provider will not shrink due to the recession. Rather they will increase because doctors in the United States will try to reduce their costs by resorting to more outsourcing. In contrast the demand for skirts and blouses will reduce-because American people will have less purchasing power. Thus Indian service providers will not be hit that badly. Yet they should try to enter new sectors and geographies. According to one report, finance-related service exports are under pressure while engineering-related service exports are growing. According to another report the share of India in service imports by Japan is mere 2 percent. The small shrinkage of service exports to the existing markets of developed countries can be more than made up by expansion in other sectors and regions. The Government must immediately create a scheme for providing subsidies for such pioneer exports. The ability lies in protactively shifting the marketing strategies. The present global meltdown can be turned into an opportunity if policy-makers play it right. Tragically enough, that is not happening in India. □□□