Creating Wealth for All

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Abstract

We have rarely if ever addressed the question of creating wealth for the masses. Most schemes for them are either based on subsidy, loan waivers or on skill building. There is some work on creating employment. All of them create income or provide doles. But there is no thinking on creating wealth for everybody. While there could be several ways of doing it, we examine this from the point of view of capital markets and how they can be more inclusive.

As the world changes rapidly, we need to step back once in a while and see how we can rethink several Institutions, including capital markets. Earlier we had State run Socialism. Private business was heavily regulated under the License Raj. The Government also owned and ran several businesses. Most people now agree that did not work – even for the stated goal of protecting the poor. Now we have something like free markets. The economy started growing from about 3% to well over 6% after that. But many are being left behind and the benefits are not reaching everybody. Critics have written about increasing inequality in India, and the absolute numbers below the poverty line have actually gone up, though the percentage has come down.

While there are several other ways of addressing the problem, we focus here on the capital markets and restructuring the capital in some enterprises. All other schemes for the masses focus on redistribution, subsidy, loan waivers and so on. There is very little talk of creating employment, and there is some action on creating a skilled work force. There are many good ideas out there. They are at best generating income but not wealth for the masses.

First of all let us look at the percent of the population that is active in stock markets. While there is no decisive study there are various estimates. They vary from 2% of the population to about 7% of the work force, which still comes to less than 3% of the total population. There are some who indirectly invest in capital markets through mutual funds. In the US, more than 50% of the population own some shares individually. There are others who invest in mutual funds. China has about 5 times the number of retail investors as India. Moreover, the ownership of stocks is skewed with a few wealthy investors, mutual funds, FIIs and some large Indian corporations owning nearly all the shares. The percentage of shares owned by retail investors in India is very low, although that number is growing fast.

We are not discussing why this is so, and what steps need to be taken to improve the reach in the volatile Indian stock markets. BSE and NSE are already working on this. We are addressing the question of increasing the assets and wealth of the masses. Even if we increase the stock market reach by a factor of two, the number of people will still be less than China and way below the US. So can we do something better?

What do the rural masses have and how can that be used to create wealth? The principal asset the rural masses have is land, mostly small holdings. Of course there are an equal number of landless poor, but that requires a different approach. Coming back to land, one recent example illustrates the point very well. Kia Motors invested more than $2 billion in Anantapur in 2017 near the Bangalore International Airport. Land prices there were about Rs. 3 to 5 lakhs per acre, and more than a thousand acres was acquired at double the market rate. So farmers got Rs.10 lakhs an acre. Within two years, the land prices have skyrocketed to over Rs. 1 crore an acre in the vicinity of the Kia motor plant. Brokers, land speculators, industries and politicians are making money on real estate there. The farmers who sold the land are not able to participate in this wealth creation. A few get Class 4 jobs in the factory. The farmers whose lands were not acquired are hoping to sell their land at a much higher price, but nearly all of it is gone or sold and today's transactions are between those who already bought land at a cheaper price.

The same is true for mining and mineral resources. People are given compensation and hopefully relocated properly. But given our inefficient Government system, not much reaches the displaced people and there are protests galore. Recently in Odisha's Niyamgiri region, the local population rejected the entry of Vedanta in a referendum and about Rs.50,000 crores of investment did not take place.

In every development project the poor lose land but don't get much share of the wealth created. Can we create transparent, tradable, well-regulated land markets? Unlike other countries, more than 50% of Indians – nearly all in rural areas – are farmers, and own land. In the US only 3% of the people are farmers, though the per capita land holding there is much higher. No other country has this situation except perhaps China. But even this may not create wealth for the masses as they would perhaps not be able to immediately take advantage of tradable land markets. Also the implications of land based trading are not clear.

Can we do better? As per Government norms, compensation for land is fixed at 200% of the actual market rate. So the investors in land – whether it is a motor company or a mining company, can give half in cash and the rest in shares, ideally at face value. The actual percentage and details can be worked out. This makes the masses participate in wealth creation as well. A farmer who sold land for Maruti in the 1980s would be very wealthy indeed if he had been given some shares in the company whose market cap today is about Rs.196,000 Crores. One share at face value Rs. 5 is now valued at over Rs.6500. The Anantapur farmers would similarly benefit from Kia Motors.

Many State Governments have given land to the Dalits. But they cannot sell that land and Indian ingenuity has invented all sorts of perverted ways of circumventing this problem. In tribal regions only tribals can own land so there is no land market. But if Dalits and tribals can participate in wealth creation as mentioned, it may be win-win for all concerned. Those displaced from Niyamgiri in Odisha for instance would not only get cash compensation but would get shares at face value in the mining enterprise. Vedanta's market cap is about Rs.65,000 crores and 1% of it in the hands of the local people can transform their lives.

Apart from land markets, and shares to the original landowners in any new enterprise, there are other ways of making capital markets more inclusive. With the new thrust on agriculture, there will be more attention to the nearly 5000 Farmer Producer Organizations (FPOs) in existence as of 2019. The membership is very low and is about 5 lakhs only. Lack of capital is one principal bottleneck that prevents growth. Even the ones that do well can only create income but not wealth as their shares can only be owned by farmers and cannot be traded in the stock market. Some countries have brought in legislation to bring in investor capital into the equivalent of FPOs (which are still called Cooperatives abroad), but in India that is not allowed. However we need to safeguard the interests of farmers and there is a key takeaway from US laws. The original promoters, like those in Google and Facebook can keep control of the company even if their share holding is diluted. With less than 20 million shares each out of nearly 700 million shares, the founders of Google control 51% of the company. A similar provision is required for FPOs. We have at least two classes of shares – one that is tradable and largely owned by outside investor capital, and the other is non-tradable and owned by farmers. Farmers can still be in control. Of course, a small percent of tradable shares can be vested with farmers as well. It will bring in capital that is scarce, bring in managerial and business talent, and allow small farmers to create wealth for themselves.

Finally a word on the landless people. Microfinance was the principal means of 'helping' them. The poor were required to save money as well in the Self Help Groups (SHGs). But they could not own any shares, which were owned by Microfinance Institutions. Here again the answer is obvious – give shares to the poor in return for their savings and/or investments. There are nearly 4 crore borrowers in the microfinance sector as of now. Bandhan Bank converted from microfinance to a small Bank. If the poor borrowers got shares at the face value of Rs.10, their shares would be worth over Rs.500. The same is true Ujjivan Financial services, and the comparable figures are Rs.10 and Rs.300. Bandhan's market cap is about Rs.65,000 crores. For a poor person, wealth can come from 2000 shares paid for at face value – that too over time and not in one shot. It is similar to employee stock options. This can transform their lives, and provide better education for their children.

A lot of details perhaps need to be worked out to implement these preliminary ideas. Rather than a rigid approach, it is better to start with a simple flexible approach. The rules can be tweaked as we gain experience over the years. There is much to be learnt from the experience of other countries in FPOs/ Cooperatives as well in start-ups.

The last question is: why should investors put their money into such ventures? A little bit of incentive for them would go a along way. Like the tax holiday for startups, we could have something similar here as well. In any case there is a lot of philanthropy and social venture capital in India and some of that money can be invested in such entities. We need to bridge the growing inequality and wealth creation is just one way we could address this problem.