The Nirav Modi Scandal*

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Nirav Modi, and his uncle Mehul Choksi, are the latest additions to the list of the so-called “entrepreneurs of new India” who have looted public money and decamped with the loot. The Punjab National Bank, the second largest bank in the country, kept giving them loans without any collateral (which is basically what happened through the complicated procedure of the so-called “Letters of Undertaking”); and one fine day Nirav Modi simply left the country with his immediate family, to be followed by his uncle a few days later.

Several characteristics are shared by all these decamping “entrepreneurs” whose list includes Lalit Modi and Vijay Mallya. First, all of them are high-profile “celebrities”. Lalit Modi for years appeared everyday on television screens in lakhs of homes across the country during IPL matches, alongside political and Bollywood heavyweights, and was hailed as the “brain” behind this event. Vijay Mallya was a member of parliament elected with much fanfare, and also a regular TV presence during IPL matches involving the team that he owned, the Royal Challengers Bangalore,. And Nirav Modi, whose diamonds adorned Hollywood and Bollywood stars, was in addition related through marriage to the country’s top “entrepreneur” family, the Ambanis.

Secondly, all of them were close to the ruling party. Lalit Modi’s proximity to Sushma Swaraj and to Vasundhara Raje continued openly even after he had fled the country. Vijay Mallya had been elected to the Rajya Sabha with the surplus votes of the BJP. And not only was Mehul Choksi “Mehulbhai” to Prime Minister Narendra Modi, but Nirav Modi actually appeared in a photograph , after having fled the country, as part of Modi’s team of Indian “entrepreneurs” at the Davos summit. The government’s subsequent claims that he merely slunk into the photograph are absurd: nobody can just slink into a Prime Minister’s photograph.

Indeed the closeness of all these persons to the ruling Party is evident from the fact that their escapes can be shown to have been “assisted escapes” by the government (as a report in The Wire establishes). In the case of Vijay Mallya, who misappropriated Rs.9000 crores, a “lookout” notice issued on October 16, 2015, was conveniently and unaccountably “downgraded” on November 25, allowing him to escape from the country on March 1, 2016. And in the case of Nirav Modi, who defrauded PNB of Rs.11400 crores, the government took no action whatsoever despite being informed about his misdemeanour in July 2016.

Thirdly, each one of them continues to be absolutely brazen about his criminal deed without an iota of remorse. Lalit Modi struts around the world pretending that he is the victim. Vijay Mallya has the temerity to march into a function at the Indian High Commission in London. And Nirav Modi has even written a letter suggesting that it is PNB’s impetuousness, leading to a media blitz on his borrowing, that is responsible for his default, ignoring conveniently that he fled the country on January 1, long before any news of his default had reached the media.

It is ironic that a government which screams its opposition to economic malfeasance, which put millions to acute hardship through an act of demonetization supposedly for fighting black money, and whose insistence on Aadhar for plugging "loopholes" in public distribution has already starved several destitute persons to death, has presided over a plunder of banks by some of the country's richest people, and even "assisted" their escape! And there is a deafening silence till now from both the Prime Minister and the Finance Minister on this latest case of plunder by Nirav Modi.

It is also ironic that Assocham should use the instance of this plunder to demand that public sector banks should be privatized! This is tantamount to a demand for handing over the banks to the very same tribe whose members are responsible for looting them: a Nirav Modi loots the PNB and sits cozily in New York, while this very loot then becomes the reason for the PNB to be handed over, say, to his relatives, the Ambanis! Or, even more ironically, the same Nirav Modi can use a front to buy the same PNB with the same money that he has looted from it!

But while Assocham can always be expected to make such outlandish demands, even the Chief Economic Advisor to the government, Arvind Subramaniam, has asked for an increase in private equity in public sector banks on the grounds that this would bring greater share-holder vigilance to check such malpractices. One wonders if his views are those of the government; and if not, then one wonders how he can freely air them while holding a responsible official post. But there are two obvious flaws in his position.

First, vigilance alone by those holding an interest in the bank cannot stop such malpractices, as the Barings Bank case shows, where the funds of Britain's oldest merchant bank were used for rampant speculation by one of its employees, Nick Leeson, which brought down the bank. In the PNB case where LOUs anyway have a very short life-span, either there was a bunching of LOUs just before the scam burst, or fresh LOUs were issued to cover expiring LOUs, so that audit could not catch the misdemeanor. The share-holders therefore could scarcely have been able to prevent it.

The more important issue here relates to the fact that lending practices were bent with impunity by a bunch of employees to favour Nirav Modi; and preventing this requires a change in practices rather than greater share-holders' vigilance. The Modi government's culpability in this case lies in not taking action despite being warned, which again calls for a change in practices. Such a change for instance, should involve greater parliamentary vigilance over PSB affairs rather than greater share-holder vigilance through privatization.

Secondly, suppose for a moment that PNB was a private bank. Then with a scam of this order, there would have been a run on the bank from depositors, leading either to its collapse with disastrous consequences, or to a government bail-out at heavy cost. But because PNB happens to be a government-owned bank, there is still enough confidence among depositors, despite Jaitley's and Modi's deafening silences, not to panic into withdrawing their deposits.

Privatization, whether involving private control or only greater private equity, will not per se prevent such occurrences, but banks will still require government funds to keep afloat in the event of such occurrences. And if government funds are to be used in such eventualities, then there is no reason why the government should not own the banks or should dilute its equity. For preventing such occurrences what is required therefore is the devising of appropriate institutional mechanisms of supervision even while retaining government ownership.

There is however a deeper problem here. Capitalism exhorts private economic agents, such as businesses, corporations and banks to pursue economic gain, indeed that is supposed to be its modus operandi; yet it wants employees of these agents to obey command and not to pursue their own private gain even clandestinely. It promotes hedonistic behavior, of maximizing gain, in the realm of the economy; but it wants the State, and its employees, not to be contaminated by such individual hedonism. It wants profit maximization by private agents, but it can work only if they do so within legal bounds; yet there is nothing to prevent them from pursuing profit-maximizing behavior at the expense of the law (through offering bribes to law-enforcers for instance).

There is in other words a basic contradiction at the heart of capitalism, namely that it is tenable only if the behaviour it exhorts is kept bounded within limits; but there is nothing in the system to keep it so bounded.

This problem has not in the past assumed the seriousness that it potentially can, because for a long time, the personnel in institutions outside of the economy, such as the State, had ideas of what is "done" and what is "not done" that were either derived from an earlier mode of production (e.g. "a sense of honour", "the badge of a public school" etc.), or, under Social Democracy, based on a certain commitment to the community-values of workers ("can't let my folks down"). In countries like ours, the legacy of the freedom struggle had introduced ethical considerations to the personnel of the State and the public sector that shunned the private aggrandizement associated with capitalism. The contradiction at the heart of capitalism in short had not assumed the intensity that would have made the system dysfunctional.

With neo-liberalism however this restraint goes. The quest for private gain gets generalized, which manifests itself in the kind of institutional break-down that we find of late. Nirav Modi's therefore is not a case of "crony capitalism" supplanting "genuine capitalism"; it is rather a case of "genuine capitalism" coming into its own and displaying its fundamental unworkability.

To be sure, having institutional restraints, as suggested above, can stem the rot for a while; but soon even these restraints themselves will get subverted, and the fundamental unworkability of a system based on the pursuit of private gain will again manifest itself.

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