Indian budget lauded by big business

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Indian big business has for the most part enthusiastically welcomed last month's budget, the second to be presented by the shaky, Bharatiya Janata Party-led coalition government. "I would rate this budget at 9, on a scale of 1 to 10," declared the chairman of Bajaj Auto, a major car and motorcycle manufacturer. "Overall it is a good budget," said Tarun Das, secretary general of the Confederation of Indian Industry. The head of India's largest private steel maker, Jamshed Irani, praised Finance Minister Yashwant Sinha for trying "to give something for everybody under very difficult conditions."

India's stock markets soared in the days following Sinha's budget speech. Investors were particularly gratified by Sinha's halving of the capital gains tax for Indians to 10 percent, exempting of mutual fund dividends from all taxation, and granting of tax breaks to the computer software sector.

Indian business also welcomed the government's efforts to boost indigenous industry by imposing a surcharge on custom duties, even while continuing to streamline and reduce tariffs. In the run-up to the budget, domestic manufacturers had pressed the BJP to assist them in competing against the transnationals. Commented Arun Gayal, director of the Academy of Business Studies, "Industry is really feeling the pinch of the liberalisation process and the fact that foreign investment has come in a big way is hitting them."

According to V.R. Panchamukhi of *Business Line*, "The Finance Minister has kept the flag of reforms flying, but with a difference, by trying to reap the nationalist wind."

The truth is, although India's economic "reform" process is now almost a decade old, India is far from the much promised "economic takeoff." There has been a significant rise in Indian exports and the upper middle class have gained access to cheap foreign consumer goods, but India has fared poorly in the competition for foreign investment. India's power generation and distribution network and its telecommunications and transport infrastructure remain mired in backwardness. Not only has the dismantling of India's nationally protected economy not provided the masses with any meaningful relief from crushing poverty, it has undercut the position of much of domestic capital. A study published last year by *Business Today* concluded that just 14 of India's 50 largest business houses are strong bets to even survive.

While Indian business has hailed Sinha's budget for balancing measures to boost indigenous capital with the need to appease foreign investors by lowering tariffs and selling off public sector enterprises, foreign capital's attitude to the budget has been far more circumspect. The International Monetary Fund has long been pressing India to reduce government spending, by slashing price and other subsidies, so as to close a budget deficit estimated to be the equivalent of 6.5 percent of GDP.

Sinha's budget does in fact predict that the budget deficit will be reduced to 4 percent of GDP in the coming fiscal year (1999-2000). However, foreign and many domestic analysts are sceptical of Sinha's claims, believing them to be based on rosy predictions of economic growth. Moreover, rather than cutting subsidies, Sinha chose to raise taxes.

For the first time since India embarked on its economic "reform" program in 1991 income and corporate taxes are being raised. The budget calls for a temporary 10 percent surcharge on income and corporate taxes, from which those in the lowest tax bracket will be exempt.

But more than half of the projected 93 billion rupee increase in tax revenue is to come from a 1 rupee per litre increase in the tax on diesel fuel. This increase, which will push up transport costs, will ultimately be passed on to consumers in the form of higher food and other prices. To try to mollify public opposition to this measure, which will rebound on the poorest sectors of Indian society, Sinha claimed that the government will use the increased revenue to finance social welfare and rural development schemes.

In his budget speech, Sinha tried to portray the income tax surcharge and the diesel tax increase as showing the government's even-handedness--all sectors of society are being asked to make sacrifices. However, the next day he told the press that the surcharge on taxes was temporary and he hoped to remove it next year. Needless to say, no similar pledge has been made in respect to the increase in the diesel tax.

The major concession Sinha offered foreign capital in his budget was a promise to speed up "public sector disinvestment", that is the selling off of public sector enterprises to investors, who will then transform them into profitable companies through job and pay cuts. Sinha boasted that in the current fiscal year the government has raised 80 billion rupees through "disinvestment" and set a target of Rs. 100 billion (or US$2.3 billion) for the coming year. He also announced that recommendations for the disinvestment of 43 public sector enterprises were already being processed by the government, and proposals to sell off several more units would soon be referred to the Disinvestment Commission. At a post-budget press conference, the finance minister insisted, "this is not phoney disinvestment. It is a genuine disinvestment."

Sinha also announced a series of measures aimed at facilitating foreign investment, including speeding up the processing of applications for regulatory approval and setting up a Foreign Investment Implementation Authority (FIIA).

Many economic and political compulsions seem to have played their role in shaping the second budget of the BJP coalition. With some 17 regionally based coalition partners, the Vajpayee government is extremely susceptible to political pressures, even from marginal interests. Due to opposition from within the coalition, the BJP was forced earlier this year to scale back an announced cut in wheat, rice, sugar, gasoline and fertiliser subsidies.

And last December several BJP allies associated themselves with a one-day general strike against the government's economic policies, involving some 20 million workers.

Fear of the reaction within the coalition and among the masses was undoubtedly a major factor in Sinha's decision not to proceed with major spending cuts. Another factor was the government's fear that a sharp reduction in public spending would push India's economy into recession.

According to most indicators, India already faces a deepening economic slowdown, due to internal pressures related to the country's dilapidated infrastructure, the fallout from the East Asian economic meltdown, and the economic sanctions imposed on India by the US and other countries following last May's nuclear tests.

In the first seven months of the 1998-99 financial year, the overall growth in industrial production was just 3.6 percent, as compared to 6.2 percent in the same period in the previous financial year. The consumer goods industry has been especially hard hit, experiencing growth of less than 1 percent and in some sectors, such as food processing and textiles, an absolute decline.

Contrary to the expectations on which the last budget was based the agricultural sector has stagnated. Food grain production is estimated to have grown by just 0.3 percent in the current fiscal year, which is well below population growth.

But it is the decline in export growth that may ultimately be the most damaging. Export growth as measured in US dollars has fallen precipitously since the mid-1990s when it hit a heady 21.1 percent (1995-96). In fiscal 1997-98 it was a meagre 1.6 percent and in 1998-99 exports will grow an estimated 0.2 percent.

The stagnation in exports may push India's trade deficit in the current financial year over $10 billion, prompting fears of a balance of payments crisis like the 1991 crisis that led India's rulers to finally opt for "liberalisation." The export shortfall certainly won't be made up by increasing foreign investment. Foreign Direct Investment in 1998-99 is estimated to be 38 percent lower than in the preceding year.

"For many analysts," wrote economist Jayati Ghosh in the February 26 *Frontline* "the key question is not *whether* India will face a balance of payment crisis, but *when*."