Indian government under renewed pressure for pro-market reforms

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Like its counterparts globally, the Indian stock market has had a turbulent ride over the past week. Amid a selling frenzy on Monday and Tuesday, shares fell to their lowest point in 14 months—having plunged 8 percent in six straight days of falls—before recovering somewhat on Wednesday and falling again on Thursday and Friday.

Software companies like TCS, Wipro and Infosys, with large exports to the US, were among the worst affected. Telecom, metal and steel stocks were also hit, reflecting concerns about slowing Indian economic growth, rising interest rates and high inflation.

The international financial turmoil, together with the prospects of recession in the US and Europe, has prompted a nervous response in Indian business circles and renewed calls for the government to press ahead with pro-market reforms.

The Reserve Bank of India (RBI) issued a statement on Monday seeking to calm the share market before it opened. Although global developments would affect the Indian economy, it declared, they were "likely to have limited impact" due to the "resilience emerging from domestic factors."

Later that day, Finance Minister Pranab Mukerjee delivered a similar message, telling reporters: "Our institutions are strong and [we] are prepared to address any concern that may arise on account of the present situation."

The market, however, ignored the reassurances. It was only after the US Federal Reserve announced a two-year continuation of its low interest rate policy that markets internationally, including in India, revived temporarily on Wednesday, before succumbing to fresh rumours about a possible downgrade of French debt.

Despite claims that India is insulated from global turmoil, the gyrations of Indian shares over the past week make clear that the economy is highly exposed to the deepening international economic crisis.

India is reliant on exports, with the monthly total rising by 82 percent year-on-year in July to $29.3 billion. The US and Europe still account for one third of Indian exports, even though the share taken by the major industrialised economies is declining. The US alone accounted for 13 percent of Indian goods and 60 percent of software exports in 2010-11.

On Thursday, finance minister Mukerjee cautiously warned that India's highly profitable information and technology industry was vulnerable to a downturn in the US, Europe and Japan. While it was "premature" to judge, he said, "there is no doubt that our IT industry may be affected."

India's top trade partner is now the Gulf Cooperation Council, with $100 billion in total trade in 2009-10. The upheavals in the Middle East will undoubtedly begin to impact on that market. Any overall decline in trade will contribute to a further slowing of the Indian economy—the growth rate is estimated to be 8.2 percent this year and 7.8 percent next year, down from 10.3 percent in 2010.

Moreover, India is dependent on an inflow of foreign direct investment, which declined by 25 percent in the fiscal year 2009-10. The inflow is currently rising sharply but is sensitive to instability in the global financial markets.

Writing in the *Hindu* this week, economic commentator C.P. Chandrasekhar highlighted India's gross public debt to gross domestic product ratio. At 66 percent, it is one of the highest in Asia. Chandrasekhar raised the spectre of the credit ratings agency Standard and Poor's downgrading Indian debt. "So if S&P needs a target to declare that some governments in the Asia-Pacific are excessively indebted, then India is in the firing line," he warned.

Facing mounting criticism from big business, the Indian government has promised to press ahead with the pro-market agenda of restructuring and privatisation, in order to open up the economy to foreign capital. That was the message delivered by Mukerjee to a conference last weekend organised by the Confederation of Indian Industry (CII) entitled "Two Decades of Reforms and the Economy Today."

Among the battery of measures being considered or implemented are: allowing foreign investors in insurance to lift their ownership share from 26 to 49 percent; reforming the present pension scheme and permitting 51 percent foreign investment in the multi-brand retail sector. The government has so far resisted foreign corporations entering the retail area, fearing the impact of the country's millions of small traders.

The government is also planning land acquisition and forest clearance bills to facilitate the provision of land for industrial development. A number of major investments have confronted determined local opposition to planned projects.

Despite the government's reassurances, big business has expressed growing frustration with the ruling Congress-led coalition. The corporate elite had expected Prime Minister Manmohan Singh, who as finance minister initiated pro-market reforms in 1991, to press ahead with its demands after winning the 2009 election and no longer having to rely on the Stalinist-led Left Front in parliament.

Indian media outlets now routinely refer to Singh as a "lame duck" prime minister, who is "in hiding." CII president B. Muthuraman recently declared: "We are waiting for some big bang announcements from the government to remove the gloom."

Late last month, a *Financial Times* article pointed to concerns that the Indian budget deficit would exceed projections by almost a percentage point. "While economists fret about loose fiscal policy, industrialists complain bitterly that the government of Prime Minister Manmohan Singh, buffeted by corruption scandals, has become so averse to making decisions that waiting times for projects to be approved and complex vetting procedures for new investment effectively signal the return to the 'licence raj', the draconian regime of controls that characterised 1970s India," it commented.

The scandals themselves reflect deep dissatisfaction in ruling circles with the Singh government, which has been weakened by furores over corrupt dealings in allocating 2G telecom licences and in the contracting for last year's Commonwealth Games in India.

Congress has been able to weather these political storms mainly because the ruling class has little faith in the main opposition party—the Hindu supremacist Bharitiya Janatha Party (BJP). The BJP, which is still tarred by the mass discontent engendered by its restructuring policies prior to 2004, was able to win only 5 of the 400 seats that it contested in recent state assembly elections.

The political paralysis in New Delhi is compounded by mounting social discontent over deteriorating living standards and the government's reform measures. Around one million bank workers stopped work on August 5 to protest against plans to open up the sector further to private banks and services. Tens of thousands of workers have been involved in strikes since the latter part of last year, especially in Tamil Nadu, over wages and conditions.

Despite a tightening of credit by the Reserve Bank of India, inflation is still on the rise—reaching nearly double digit figures. Food price rises are even higher, severely affecting the three-quarters of India's population that survives on less than $2 per day.

Resistance is also spreading to the rural areas. Last month, the government was forced to suspend the acquisition of 1,600 hectares of land for a major industrial project, due to protests by local villagers. This stand-off over a $12 billion steel plant to be built by South Korea's POSCO corporation in the eastern Indian state of Orissa has been ongoing for five years.

The government is acutely aware that as it bows to big business demands for further pro-market restructuring and austerity measures, it threatens to trigger a social eruption that would dwarf those that have taken place in the Middle East.