# Storm clouds gather over Indian economy

**Kranti Kumara**
**3 May 2012**

The mood of India's political and economic elite has darkened in recent months. Not only has growth slowed, even as inflation surges ahead at a near double-digit pace. A sharp increase in the country's fiscal deficit and a yawning current accounts deficit have raised fears that India could be roiled by capital flight or even a balance of payment crisis akin to that of 1991, when India, facing state bankruptcy, was forced to airlift its gold reserves abroad to secure emergency IMF loans.

The possibility of a 1991-type crisis was directly raised by D. Subbarao, the head of India's central bank, the Reserve Bank of India, during an economic forum in New Delhi in the middle of April.

With Prime Minister Manmohan Singh in the audience, Subbarao compared several key contemporary economic indicators with those of 1991.

In 1991 the fiscal or central government budget deficit was equal to 7 per cent of Gross Domestic Product (GDP), whereas in the fiscal year that ended in March, it is projected to have been equivalent to 5.9 per cent of GDP. The current account deficit is at 3.6 per cent of the GDP, which is higher than in 1991. Short term external debt (this includes both government and non-governmental debt) is even worse at 23.3 per cent of GDP versus 10.2 per cent in 1991.

"That is quite a disturbing picture," conceded Subbarao. "Nevertheless," he continued, "I would still argue that in 1991, an implosion was imminent. In 2012, an implosion is not imminent."

What is indisputable is that India is beset by mounting economic problems and that the world capitalist system is in the throes of its longest and most convulsive crisis since the Great Depression.

In the just completed 2011-12 fiscal year, India's budget deficit (the difference between government revenue and total expenditure) was Rs. 5.22 trillion (over $100 billion), equal to about 40 percent of the central government's total expenditure, and at an expected 5.9 percent of GDP, far higher than the government's deficit-to-GDP target of 4.6 percent.

For the April 2012-April 2013 fiscal year, the Finance Ministry is projecting a decline in the deficit-to-GDP ratio to 5.1 percent, as a result of economic growth, spending cuts—particularly on fuel and fertilizer price subsidies—and increased revenue from disinvestment (privatization) of public sector units.

However, most financial analysts do not believe the government's claims that it will be able to slash the deficit-to-GDP ratio by almost one percentage point in the coming year and to below 4.5 percent in the 2013-14 fiscal year.

To begin with, the growth rate has slowed. And with the European Union the single largest recipient of Indian exports in economic turmoil, there is little reason to believe it will soon bounce back.

In 2011-12 GDP growth fell to 6.9 percent, a drop of 1.5 percent from the previous year. While the Finance Ministry claimed in the budget delivered two months ago that India's economy will grow 7.6 percent in the current fiscal year, the credit rating agency Standard and Poor's is predicting GNP growth of just 5.3 percent.

India's current account deficit (the gap between all incoming and outgoing trade, services and monetary transactions) has been widening at an alarming rate due to a mounting trade deficit and a decline in foreign investment. During the first three-quarters of the 2011-12 fiscal year, the current account deficit increased by $43 billion.

This in turn has placed pressure on India's foreign exchange reserves. In 2008, India had reserves of $315 billion enough at that time to pay for 13 month's worth of imports. Today it has reserves of $294 billion, which is sufficient to pay for 7.5 months of imports.

A significant factor in India's trade and current

© World Socialist Web Site

accounts deficit is the high price of oil, as India imports 80 percent of its oil. But even excluding oil, imports are rising more rapidly than exports. While India increased its exports by 21 percent in the 2011-2012 financial year, its imports grew by 32 percent, contributing to an increase in the trade deficit to $185 billion.

Citing the increasing size of the fiscal deficit and the government debt-load, Standard and Poor's (S&P) recently downgraded India's sovereign debt outlook from "stable" to "negative." The agency also warned that there is a 33 percent chance of a downgrade in the country's debt rating from the lowest possible "investment grade" rating to a "junk grade" designation. S&P's move means that the Indian government will have to pay higher interest charges and, should it and other credit rating agencies slash India's credit rating, much higher. In 2011-12 India's interest burden amounted to Rs. 2.8 trillion ($53 billion), equal to more than a third of the government's total revenue of Rs. 8 trillion ($153 billion).

S&P's announcement caught the Indian government and elite completely off-guard. The *Times of India* reported that Finance Minister Pranab Mukherjee's first public comment was that "there is no need to panic," but noted wryly that this was aimed more at his own ministry than the general public.

"[We] deserve better ratings than countries like Tunisia," said a miffed Finance Ministry official after the downgrade—a reference to the fact that India's credit rating ranks with that of Tunisia, a country whose economy is in turmoil following the overthrow of the US-backed dictator Ben Ali in early 2011.

In a revealing picture of the power these credit-rating agencies wield over national governments, the *Times of India* reported that two weeks before the downgrade, Indian Finance Ministry officials pulled out all stops when S&P's Singapore-based analyst Takahira Ogawa visited New Delhi. Citing India's supposedly bright economic prospects, they sought to convince Ogawa that India's credit rating should be upgraded.

Instead, S&P, speaking on behalf of international capital, chastized India's Congress Party-led coalition government for not making good on its promises to slash social spending and implement a new series of pro-big business "reforms" due to popular opposition.

"We expect," said the S&P report justifying putting India on a credit-watch, "only modest progress in fiscal and public sector reforms, given the political cycle—with the next elections to be held by May 2014—and the current political gridlock. Such reforms include reducing fuel and fertilizer subsidies, introducing a nationwide goods and services tax, and easing of restrictions on foreign ownership of various sectors such as banking, insurance, and retail sectors."

In response to the S&P announcement, India's government scrambled to demonstrate its commitment to such "reforms," with Prime Minister Manmohan Singh announcing his government's intention to hike the price of petrol and deregulate diesel fuel. The latter is used heavily by railways and trucks, so increases in the cost of diesel fuel quickly translate into food price rises. As it is, food prices have been rising sharply since 2008, further squeezing the three-quarters of the population who survive on $2 or less per day.

Like its rivals in Europe, North America, and elsewhere in Asia, the Indian bourgeoisie is determined to make the working class and toilers pay for the capitalist crisis.

Moreover, notwithstanding the bombast of the Indian bourgeoisie, India, with its growing dependence on foreign borrowings to finance its fiscal deficit and large and rising current accounts deficit, is increasingly vulnerable to capital flight and a European-style sovereign debt crisis.

To contact the WSWS and the Socialist Equality Party visit:

**wsws.org/contact**

© World Socialist Web Site